



Australian Government
Inspector-General of Taxation

Debt Collection

A report to the Assistant Treasurer

Inspector-General of Taxation

July 2015

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3 July 2015

The Hon Josh Frydenberg MP
Assistant Treasurer
Parliament House
Canberra ACT 2600

Dear Minister,

Debt Collection

I am pleased to provide you a copy of my most recent review into the Australian Taxation Office's (ATO) management of Debt Collection. The executive summary provides a snapshot of the issues and recommendations made to the ATO.

Although all 19 recommendations were made to the ATO, the ATO believes that they are unable to implement Recommendation 3.3 without seeking Government's consideration of the matter.

I am grateful for the support, contribution and willingness of those who provided their time, expertise and experience in the conduct of this review.

Yours faithfully,

A handwritten signature in dark ink, appearing to read 'Ali Noroozi', with a long horizontal stroke extending to the right.

Ali Noroozi
Inspector-General of Taxation

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EXECUTIVE SUMMARY

The Inspector-General of Taxation's (IGT) Debt Collection review was prompted by concerns raised by individuals, small businesses, tax and insolvency practitioners as well as their representative bodies. Broadly, these concerns related to the Australian Taxation Office's (ATO) ability to recover tax debts effectively whilst ensuring that its actions were proportionate to circumstances of the affected taxpayers.

The continual growth in collectable tax debt over the last decade to more than \$20 billion in 2013-14 and its potential impact on government services were also important considerations in undertaking this review. The ATO has acknowledged that its previous approach to debt collection was 'random and ad hoc' and had not reduced its overall growth. Such an approach involved a linear process for debt recovery which generally relied upon a series of escalated actions. Prior to the commencement of this review, the ATO had begun developing a program of work to explore alternatives and improve its recovery action.

Furthermore, it is not uncommon for the ATO to initiate additional remedial programs in anticipation of IGT reviews. The IGT supports such action where improvements are realised more quickly for the tax system and stakeholders alike. In these circumstances, the IGT takes a cooperative approach to assist the ATO in improving its strategic focus and achieve optimal outcomes.

Given that the ATO's new program of work will take some time to be fully implemented and bear fruit, the IGT has made a number of recommendations as interim measures. One of these measures proposes a focus on the main debt holdings which are owed by individuals and micro businesses. These two taxpayer segments account for approximately 60 per cent (\$12.3 billion) of total collectable tax debt. Related recommendations have also been made to identify underlying causes of cash flow and payment difficulties for these taxpayers and to develop preventative strategies. Another interim measure proposes that the ATO take more frequent and proportionate debt recovery action to minimise the necessity to take firmer action at a later time.

The IGT has also considered the ATO's developing projects or programs as well as its previous approaches. However, it is important to appreciate that, as key projects were at various stages of design, development and implementation, their effectiveness cannot be comprehensively assessed. The IGT has assessed these projects to the extent possible, has supported certain of their features and recommended enhancements with respect to others in order to reduce overall debt whilst ensuring recovery actions are proportionate and that taxpayers are treated fairly.

The ATO's new overarching strategic focus is to design actions that reduce overall debt holdings by using taxpayer behavioural analysis to prevent debts arising and, where they do arise, taking the most effective recovery action at the most appropriate time. This is consistent with recommendations made in previous IGT reviews where the use of behavioural analysis is a common theme. The IGT continues to endorse such an approach.

However, the IGT has identified a need to ensure ATO officers have the appropriate level of expertise and experience to handle taxpayer cases and fulfil procedural requirements. The ATO has a framework for officer decision authorisations and also provides training and support for various aspects of debt recovery. The decisions of officers, who are considered 'proficient', are not scrutinised in the majority of low risk debt cases. For example, a junior ATO officer considered proficient may garnish up to \$50,000 from taxpayers' bank accounts. Given the sustained and substantial level of individual taxpayer complaints to the Ombudsman and the IGT over the last decade, particularly in relation to ATO garnishee actions, the IGT believes that there is a need for greater top-down supervision. Accordingly, the IGT has recommended a range of improvements, including expanded team leader approval requirements and training on commercial awareness, improved guidance and decision making support tools as well as better assurance of staff adherence to policies.

The broader impact of the ATO's debt recovery actions on other creditors was also considered by the IGT. Such impact may occur where taxpayers are either unable to pay their creditors or make delayed payments. The delayed or non-payment may, in turn, cause financial difficulties for their creditors. Indeed, a third-party survey reported that many small businesses have entered some form of insolvency administration. In another survey, over one-third of respondents had a supplier or customer who was unable to pay creating a domino effect of financial difficulty. Accordingly, the IGT is of the view that the ATO has a role to support the broader economy in terms of the impact of its action on third party creditors. In this respect, the IGT has recommended that the ATO should develop improved metrics to better assess its performance and the benefit to the economy.

In relation to the ATO's engagement of external debt collection agencies to assist with debt recovery, some stakeholders fundamentally opposed it. The IGT has recommended that the ATO better inform and educate the public by providing information on its use of external debt collection agencies both to assuage concerns and to make transparent the intended benefits and outcomes.

Overall, the IGT has made 19 recommendations to 16 of which the ATO has agreed, agreed in principle or agreed in part. The ATO has disagreed with 2 recommendations and considered that 1 recommendation was a matter for Government.

The IGT seeks the highest levels of transparency in reporting recommendations and the ATO responses. Whilst ATO's agreement with many of the recommendations is welcomed, the ATO's associated commentary, on this occasion, raises potential governance concerns as it creates substantial uncertainty with the scope of agreement and risks inadequate implementation of recommendations. Furthermore, elements of recommendations are not addressed or the ATO appears to be effectively disagreeing with them. For example, the ATO has agreed with Recommendation 4.8 which is aimed at improving staff supervision and decision making. However, the ATO's commentary appears to limit its agreement to pre-existing arrangements and does not address the part of the recommendation aimed at improving the supervision of junior staff who issue garnishee notices.

In relation to disagreed recommendations, the ATO has disagreed with Recommendations 4.5 and 4.7. The former seeks to make taxpayers aware of their right to request that the ATO exercises its discretion to not offset tax credits against debts at the outset of discussions. Recommendation 4.7 requires the ATO to consider merging the Debt Business Line into the Compliance Group. While the ATO has disagreed with it, the accompanying commentary confirms that consideration of the appropriate organisational structure will be undertaken through its 'Reinvention' program.

The ATO has disagreed in part with two recommendations. These are 3.1(b), relating to the development of streamlined viability and capacity to pay tools for use in lower risk cases, and 4.1(d) which proposes the adoption of a unified approach between debt and legal officers when issuing garnishee notices in disputed debt cases.

The ATO response to Recommendation 3.3 is that it is a matter for Government to consider as the ATO believes the legislative policy prevents it from remitting interest in appropriate cases to encourage prompt payment of debts.

It should be noted that the recommendations are an integrated package where each builds upon the other. As the ATO has disagreed or effectively disagreed with certain recommendations or aspects thereof, the full benefit of the intended integrated outcome may not be realised.

Given the importance of the management and collection of debts in the tax system, the IGT will maintain a watching brief over the effectiveness of the ATO's program of change. As future complaint cases may also surface issues, the IGT will appropriately explore and address these issues through discrete and targeted investigations.

LIST OF RECOMMENDATIONS

RECOMMENDATION 2.1

The IGT recommends that the ATO incorporate the following initiatives into its Analytics for Client Engagement Program or related projects aimed at minimising tax debt:

- (a) a program to identify the underlying causes of cash flow and payment difficulties for micro business and individual taxpayers and develop preventative strategies;*
- (b) an online facility which taxpayers and their advisers can use to prepay anticipated tax debts – for example through the myGov website and Tax Agent Portal;*
- (c) facilitate discussions with software developers, insolvency practitioners and small business advocates to promote the benefits of incorporating the business performance review tools (such as the ATO's Business Viability and Assessment Tool) into commonly used accounting software;*
- (d) make publicly available a personal financial management tool such as the Debt Serviceability Tool; and*
- (e) identification of taxpayers who are most likely to experience cash flow difficulties and encourage them to seek professional advice.*

RECOMMENDATION 2.2

The IGT recommends that the ATO, as it designs and implements new debt strategies:

- (a) continue to use existing research findings to target debt activities to those taxpayer segments which comprise substantial amounts of recurrent and/or aged tax debts, such as micro businesses and individuals; and*
- (b) incorporate feedback loops to facilitate continuous improvement.*

RECOMMENDATION 2.3

The IGT recommends that the ATO:

- (a) better inform the public about its debt strategy by, for example, publishing its approach to debt collection, including any changes or modifications thereto; and*
- (b) as an interim measure, whilst awaiting the result of its research projects, take earlier, more frequent and proportionate debt recovery action to minimise the necessity to take firmer action at a later time.*

RECOMMENDATION 2.4

The IGT recommends that the ATO:

- (a) jointly develop with other relevant agencies, a suite of educative materials for small business owners on their legal responsibilities; and*
- (b) continue to implement and refine the integrated risk treatment plan, for phoenix activity across the organisation, which incorporates the new inter-agency powers, engagement with intermediaries and assessment tools for measuring the success of the plan.*

RECOMMENDATION 2.5

The IGT recommends that the ATO:

- (a) publish further statistical information and analysis, currently only available internally, to better inform the public about tax debt and strategies to address them; and*
- (b) undertake further statistical analysis to develop improved metrics, which are reported publically, to better describe the effectiveness of its debt strategies in relation to such issues as improving payment on time, payment behaviour over the longer term and the benefit to the economy.*

RECOMMENDATION 3.1

The IGT recommends the ATO:

- (a) expand its new training framework to include programs aimed at improving the commercial awareness and understanding of taxpayer behaviours for those staff who make decisions with respect to payment arrangements; and*
- (b) develop streamlined viability and capacity to pay tools which incorporate industry benchmarks for use in lower risk debt cases.*

RECOMMENDATION 3.2

The IGT recommends the ATO:

- (a) consult with relevant government agencies to more appropriately identify the contemporary nature of 'serious hardship' and to use appropriate tools in identifying individual cases;*
- (b) review its guidance and publications to make the circumstances clearer as to where a release is likely to be granted and where it may not be granted for 'serious hardship' cases (including system procedures for staff decisions, such as alternatives to release).*

RECOMMENDATION 3.3

The IGT recommends the ATO:

- (a) engage with taxpayers in discussions on remission of interest as a means of supporting prompt payment of debt by, for example, including on payment reminders that partial remission may be granted where debts are paid promptly; and*
- (b) based on the findings of its research into 'tipping points' and the 'next best action' consider remitting interest in appropriate cases to further encourage prompt payment.*

RECOMMENDATION 4.1

The IGT recommends that the ATO improve the process for issuing garnishee notices by:

- (a) developing improved processes to correct data mismatches between the ATO Integrated System and Receivables Management System;*
- (b) encouraging financial institutions to challenge garnishee notices where they believe notices may have been issued to the incorrect bank account;*
- (c) reviewing its officers' adherence to policy of making every effort to telephone taxpayers, particularly lower risk taxpayers; and*
- (d) adopting a unified approach between debt and legal officers when issuing garnishee notices for all cases.*

RECOMMENDATION 4.2

The IGT recommends that, consistent with recommendation 2.3(b), the ATO act sooner and take proportionate actions to prompt company directors to address impending insolvency.

RECOMMENDATION 4.3

The IGT recommends that the ATO amend its processes for issuing Departure Prohibition Orders to require Second Commissioner approval and that SES officers be ultimately responsible for the maintenance of DPOs.

RECOMMENDATION 4.4

The IGT recommends that the ATO formalise the authorisations required to take security over assets and allocate these authorisations to appropriately senior officers.

RECOMMENDATION 4.5

The IGT recommends that, where the criteria for offsetting credits against debts are met, the ATO provide guidance to staff to inform taxpayers of their right to request the discretion 'not to offset' be exercised at the outset of discussion relating to, for example, disputed debt or payment arrangements.

RECOMMENDATION 4.6

The IGT recommends that the ATO incorporate into its procedures and guidance the need to consider the impact of its actions on other creditors as it pursues tax debts.

RECOMMENDATION 4.7

The IGT recommends the ATO consider merging the Debt Business Line into the Compliance Group.

RECOMMENDATION 4.8

The IGT recommends that the ATO:

- (a) improve Debt Business Line team leader supervision of staff including requiring team leader approvals in appropriate cases;*
- (b) align case allocation systems with the debt staff capability matrix once developed;*
- (c) implement a network of advisory staff in the Debt Business Line to support escalation of issues, development of precedents and an effective database of debt decisions; and*
- (d) improve the enforcement of recording details of debt cases on its systems to promote better management of particular lower risk cases.*

RECOMMENDATION 5.1

The IGT recommends that the ATO measure and publish information relating to the performance of External Debt Collection Agencies, including the use of benchmarking, on aspects such as the:

- (a) efficiency of the pursuit of collectable debt;*
- (b) sustainability of payment arrangements; and*
- (c) impact on taxpayers and their long-term payment compliance behaviour.*

RECOMMENDATION 5.2

The IGT recommends the ATO:

- (a) publish the types of debt collection work for which it engages External Debt Collection Agencies and the types of cases referred to them; and*
- (b) provide External Debt Collection Agencies with more frequent estimates of the volume of cases to be referred so that they can better manage resources and meet performance obligations.*

RECOMMENDATION 5.3

The IGT recommends the ATO:

- (a) better inform the public about External Debt Collection Agencies' role particularly in relation to how they are required to act with respect to disputed debts, enter into payment arrangements and remit interest;*
- (b) increase taxpayer awareness on how they can make complaints about the actions of External Debt Collection Agencies from the outset; and*
- (c) assist External Debt Collection Agencies to give more consideration to taxpayers' circumstances.*

CHAPTER 1 – BACKGROUND

OVERVIEW OF STAKEHOLDER CONCERNS

- 1.1 During public consultation for the Inspector-General of Taxation's (IGT) 2013–14 work program, stakeholders raised concerns with the Australian Taxation Office's (ATO) approach to debt collection including delayed recovery action, disproportionate action when debts were pursued and the use of external debt collectors. The IGT commenced this review in response to these concerns.¹
- 1.2 The IGT called for and received a number of submissions and also met with taxpayers, tax practitioners, insolvency practitioners and their representative bodies as well as External Debt Collection Agencies (EDCA) to gain a better understanding of the issues and identify areas requiring improvements.

A range of concerns were raised by stakeholders which may be grouped into the following themes, the ATO's:

- debt strategies to address the growth in tax debt, including whether the ATO could better prevent debts from arising, improve targeting of debt activities and commence such activities earlier and proportionate to taxpayers' circumstances;
 - debt assistance activities, including how the ATO determines eligibility for payment arrangements, remission of interest and penalties as well as its debt release for serious financial hardship;
 - debt recovery activities, including how the ATO administers activities, such as garnishee notices, Director Penalty Notices (DPN), Departure Prohibition Orders (DPO), freezing orders (Mareva injunctions), securities, tax credit offsets and insolvency actions as well as the recovery of disputed debts and the accuracy of information on which the ATO relies; and
 - use of EDCAs.
- 1.3 The above concerns are discussed in more detail in the subsequent chapters. ATO debt management strategies are explored in Chapter 2 whilst ATO debt payment assistance, ATO former debt recovery activities and ATO use of EDCAs are examined in Chapters 3, 4 and 5 respectively.
- 1.4 Before addressing stakeholders' concerns, it is beneficial to first understand a range of factors including business cash flow management, credit risks, how debts arise in the tax system and how the ATO manages collection activities.

1 The review was commenced pursuant to section 8(1) of the Inspector-General of Taxation Act 2003. The terms of reference for this review issued on 26 May 2014, which are reproduced in Appendix 1.

CASH FLOW MANAGEMENT AND CREDIT RISK

- 1.5 There are a range of reasons why taxpayers may not be able to pay their debts when they become payable. A recently released Australian Securities and Investments Commission (ASIC) report reveals the top three causes of company failure as follows:
- poor strategic management of business (42 per cent);
 - inadequate cash flow or high cash use (41 per cent); and
 - trading losses (32 per cent).²
- 1.6 Many businesses identify cash flow as the issue most likely to impact their operations ahead of wages, interest rates, fuel prices, access to credit and the strength of the Australian dollar.³ It is also commonly accepted that recently established small businesses have a relatively lower survival rate than larger businesses.⁴ Many new businesses may face financial pressures. For example, after the first financial year of trading, they are required to lodge an income tax return and shortly thereafter, make the first incremental prepayment under the Pay As You Go (PAYG) Instalment system. At this time, new businesses are put under additional financial pressure as they have to satisfy tax liabilities with respect to two financial years in close succession.
- 1.7 In an analysis of invoice payments, a debt recovery firm, Dun and Bradstreet (D&B), also found that on average, the time taken to pay debts in Australia has slowed to its lowest rate in three years. It was suggested that the slowing in payment times is evidence that businesses are facing cash flow pressures and difficulty in managing their finances.⁵ This concern has been echoed in other countries.⁶ A summary of the D&B survey findings is presented below:

2 ASIC, *Report 372: Insolvency Statistics: External Administrators' Reports* (July 2012 to June 2013) (2013) p 7. It should be noted that there may be multiple causes, hence why the sum of the percentages is greater than 100 per cent.

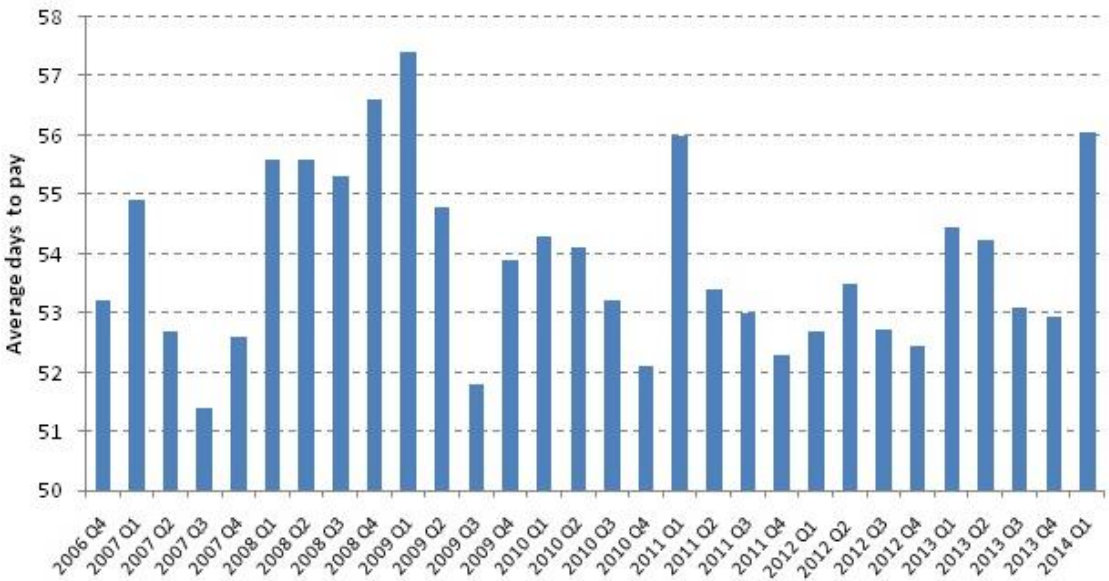
3 Dun and Bradstreet, *Businesses facing cashflow squeeze* (2014) <<http://dnb.com.au>>.

4 Reserve Bank of Australia, *Small Business Finance Roundtable* (2012) p 7.

5 Dun and Bradstreet, above n 3.

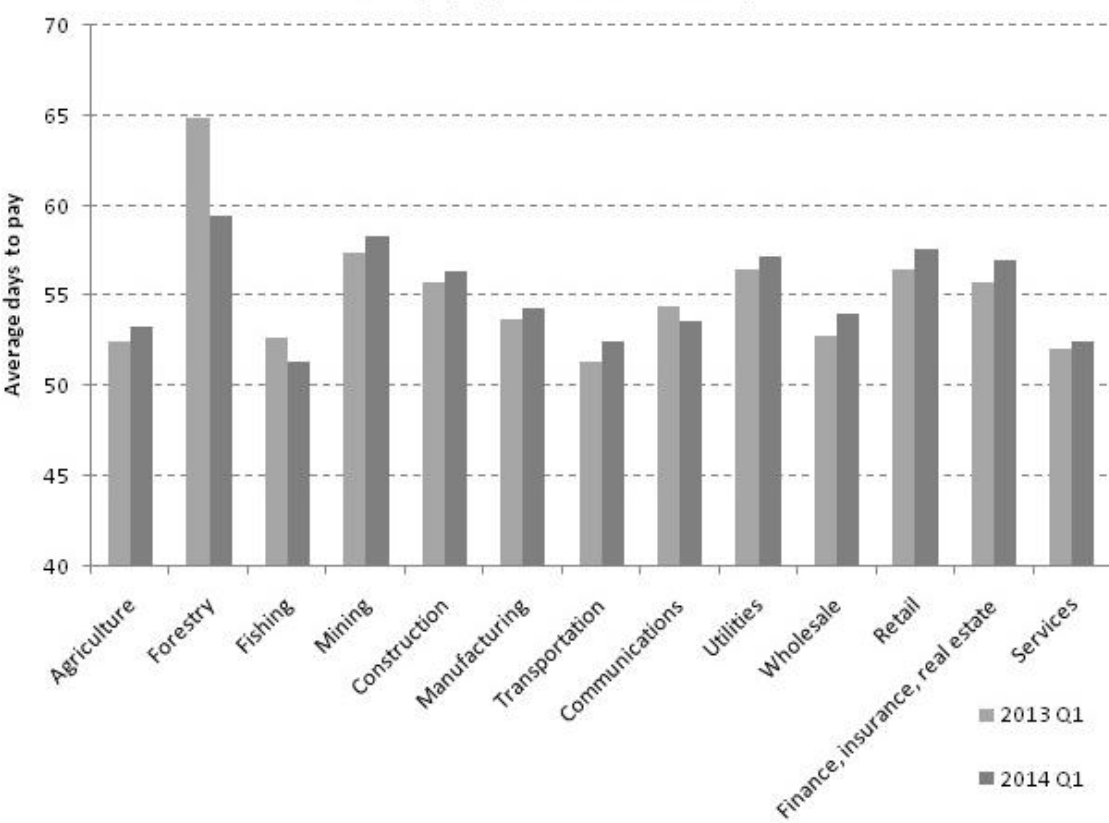
6 Serena Ng and Cari Tuna, 'Big Firms are Quick to Collect, Slow to Pay', *Wall Street Journal* (online), 31 August 2009 <<http://www.wsj.com>>.

Figure 1.1: Average payment times

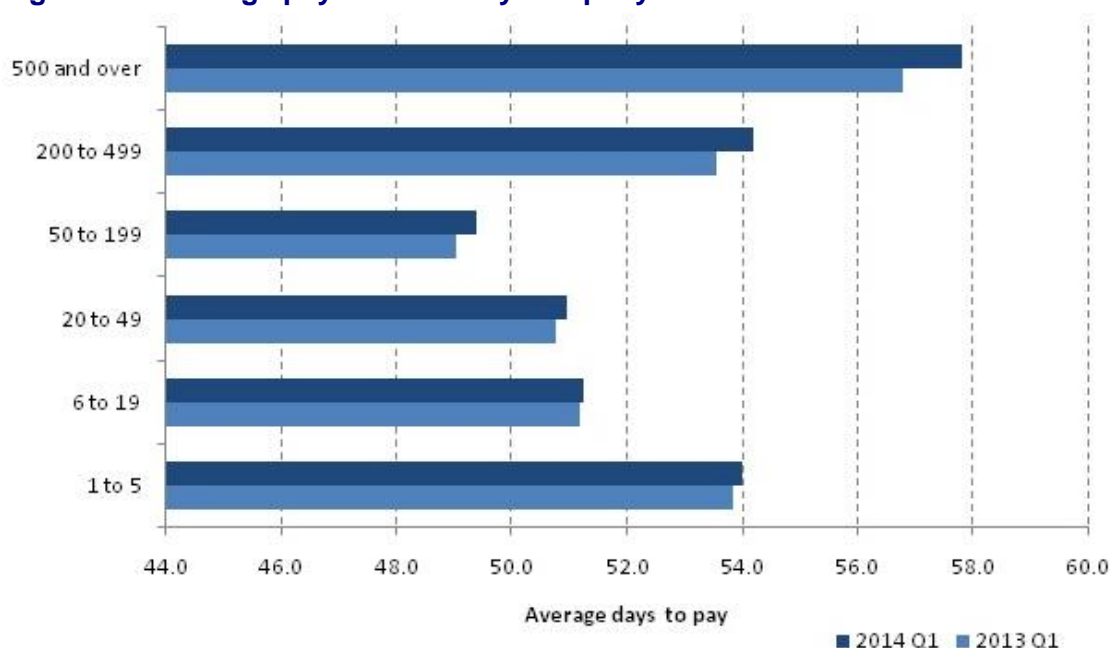


Source: D&B.

Figure 1.2: Average payment time by industry



Source: D&B.

Figure 1.3: Average payment time by company size

Source: D&B.

- 1.8 The above figures show that there has been an increase in average payment times. Such increase is approaching that observed during the peak of the Global Financial Crisis (GFC) in 2008–09. Primary (forestry and mining) and secondary industries (utilities, construction, retail and finance) seem to be the most affected. Moreover, it appears that larger businesses and micro businesses have the slowest average payment times. This lends support to the submission by the Australian Small Business Commissioner (ASBC) to the Government’s ‘Prompt Payment Protocol’ (Protocol) to address the culture of late payments. The ASBC submission states that the Protocol needs to be supported by all sectors of the business community. The submission recognises that whilst there are obvious benefits for small business, which are often more vulnerable than larger business within the supply chain, the Protocol should not be about ‘big versus small’ or making a particular sector accountable.⁷
- 1.9 When businesses begin to experience cash flow difficulties, they may reprioritise payments to some debtors and attempt to negotiate extended payment timeframes with others. The late payment of such debts affects the cash flows of creditor businesses that also need to cover their own operating costs, which in turn delays how quickly they can pay their own creditors and suppliers. In the D&B Survey, it was found that trade creditors are the most vulnerable to late or missed payments as 48 per cent of respondents would opt not to pay their suppliers if they were unable to pay all their expenses on time ahead of other expenses, such as utilities, rent/mortgages and bank loans.
- 1.10 When a business’ cash flow and debts become unmanageable, insolvency action may be the only reasonable action for a creditor to recover some of the debts owed to them.

⁷ Australian Small Business Commissioner, Submission to the Department of Industry, Innovation, Climate Change, Science, Research and Tertiary Education, *Prompt Payment Protocol*, August 2013 <<http://www.asbc.gov.au>>.

- 1.11 The D&B Survey also found the impact of cash flow difficulties may be widespread as, during the 2013 calendar year, 34 per cent of respondents to their survey had a supplier or customer who became insolvent or was otherwise unable to pay them.⁸ In another survey conducted by Jones Partners, it was observed that corporate insolvencies have continued to grow with approximately 10,000 businesses entering some form of insolvency administration each year. Furthermore, over 80 per cent of these entities are family-owned Small to Medium Enterprises (SME) employing less than 20 workers. Similarly, personal insolvencies have also continued to grow affecting approximately 30,000 individuals every year.⁹
- 1.12 Changes in the rate of insolvency are suggested by some commentators to be reflective of a number of underlying economic factors, including the economic environment, industry structure, access to credit, extent of leverage and the availability of voluntary avenues to deal with insolvency.¹⁰

Financial institutions' approach to debt

- 1.13 Many businesses may trade on a basis where the terms of payment specify a payment date after goods or services have been invoiced and supplied. Such payment terms are akin to a form of financial accommodation and assists businesses manage their cash flows. However, delayed payment terms also create a risk of payment default.
- 1.14 Financial institutions commonly provide financial accommodation. However, unlike many other businesses, they manage potential payment default, the resulting disruption to cash flow and associated collection costs by assessing the credit risk of debtors. Credit risk assessments are important for financial institutions to manage their credit risk exposure for individual transactions as well as across their entire portfolio to ensure that they have adequate capital backing and that they are adequately compensated for risks incurred.¹¹
- 1.15 'Risk-based pricing' through interest rates and other fees are used to compensate financial institutions for the credit risk they hold. Generally, financial institutions will charge a higher interest rate to borrowers who are more likely to default on payment or who are unable to provide adequate security.¹²

8 Dun and Bradstreet, above n 3.

9 Jones Partners, *Insolvency Report 2014: Insolvency activity & the state of the national economy – the past, present and future* (2014) <<http://www.jonespartners.net.au>>.

10 Ibid.

11 Basel Committee on Banking Supervision, *Principles for the Management of Credit* (2000).

12 J E Ingersoll, 'Interest Rates' in John Eatwell, Murray Milgate and Peter Newman (eds), *The New Palgrave Dictionary of Economics Online* (Palgrave Macmillan, 2015); Investopedia, *Interest Rate* <<http://www.investopedia.com>>.

Economic considerations

- 1.16 A free and healthy competitive environment and a dynamic SME sector is considered by some commentators to be vital to the Australian economy.¹³ This competitive environment has an element of ‘only the fittest will survive’ as many SMEs may fail causing financial hardship for owners, workers and creditors. However, this also demonstrates a robust appetite for commercial endeavour and entrepreneurship.¹⁴ For this reason, commentators believe that it is important that there continues to be appropriate incentives to start a business, including a framework which allows cost effective options for owners to manage their company during financial distress whilst also providing appropriate outcomes for creditors and other parties. Such frameworks for dealing with company or personal financial failure seem necessary, particularly as weaknesses across the Australian economy persist according to some commentators.¹⁵
- 1.17 Some consider that for entrepreneurship to flourish, certain preconditions are necessary. These include efficient financial markets, a simple and transparent corporate taxation system, labour market flexibility and insolvency and bankruptcy regimes which are adapted to the realities of the business world. In this sense, they believe that government should create robust and predictable institutional and tax environments that enable trouble free entry of new ventures and expedite the exit of failed ventures.¹⁶
- 1.18 During an economic downturn, it is generally expected that tax compliance risks, will grow together with the need for greater taxpayer support. However, ‘tolerating’ non-compliance is not considered an appropriate response to economic difficulty because it is distortionary, inequitable and hampers the rebuilding of the tax base over the medium term.¹⁷ Some commentators recommend that in such circumstances, the focus should be on containing non-compliance but also helping taxpayers to cope with financial distress by:
- expanding assistance;
 - focusing enforcement on the highest revenue risks;
 - ensuring legislation facilitates administration; and
 - improving communication and community outreach.¹⁸

13 Jones Partners, above n 9.

14 Ibid.

15 Ibid.

16 The Treasury, *Budget 2014-15: Budget Paper No. 1* (2014) [Statement 2: Economic Outlook].

17 John Brondolo, ‘Collecting Taxes During an Economic Crisis: Challenges and Policy Options’ (Staff Position Note SPN/09/17, International Monetary Fund, 14 July 2009).

18 Ibid.

TAX DEBT

- 1.19 'Taxation' is generally considered to be a compulsory payment raised for Government and public purposes. It is not a payment for services rendered or a penalty, the extraction of which is not arbitrary and the liability for which is not incontestable.¹⁹
- 1.20 Raising revenue through taxation to fund Government activities and public purposes, such as welfare and defence, is a fundamental feature of modern societies.²⁰ Indeed, it has been said that 'taxes are what we pay for a civilised society'.²¹
- 1.21 The ATO is responsible for managing the tax and superannuation systems as well as optimising the collection of the vast majority of the Commonwealth's revenue.²² Accordingly, the way in which the ATO collects taxes may impact upon Government policy and services for Australians as well as the operation of commercial enterprise and the broader economy.
- 1.22 The ATO calls for the lodgment of annual income tax returns²³ requiring taxpayers to provide relevant information to quantify the tax to be collected. For full self-assessment taxpayers, such as companies, corporate unit trusts, public trading trusts and superannuation funds, the lodged return is deemed to be an assessment. From 1 July 2012, this approach was extended to indirect taxes. For partial self-assessment taxpayers, such as individuals, the ATO uses the information in their tax return to ascertain the amount of taxable income and tax payable. A 'Notice of Assessment' (NOA) containing this information is then issued to the taxpayer.²⁴
- 1.23 Certain taxpayers' liabilities are also collected, for example, through the PAYG system for salary and wages following the lodgement of an Instalment Activity Statement (IAS).²⁵ For Goods and Services Tax (GST) purposes, it is collected through a Business Activity Statement (BAS)²⁶.
- 1.24 A Running Balance Account (RBA) is used by the ATO to record liabilities and payments made on a single account for each taxpayer.
- 1.25 In relation to a BAS or IAS, the ATO updates the taxpayer's RBA to record any liability amounts or payments made. If the amount of tax paid throughout the year exceeds the tax assessed, the taxpayer may be entitled to a refund. If insufficient tax has been paid the ATO will advise the taxpayer of the outstanding tax payable.

19 *Matthews v The Chicory Marketing Board (Vic)* (1938) 60 CLR 263, 276 (Latham CJ); *Australia Tape Manufacturers Association Ltd v Commonwealth* (1993) 176 CLR 480, 501; *MacCormick v FCT* (1984) 15 ATR 437, 446; *DCT (Qld) v Truhold Benefit Pty Ltd (No 2)* (1985) 16 ATR 466, 469; *Airservices Australia v Canadian Airlines Int'l Ltd* (1999) 202 CLR 133, 178.

20 *R v Barger* (1908) 6 CLR 41.

21 *Compania de Tabacos v Collector* 275 US 87 (1904).

22 ATO, *Strategic Intent* (2014) pp 3-4, 6, 8; Chris Jordan, 'Reinventing the ATO – Building Trust in Australia's Tax Administration' (ATAX 11th International Tax Administration Conference, Sydney, 14 April 2014); R L Deutsch et al, *Australian Tax Handbook* (Thomson Reuters, 2014) [1 350].

23 *Income Tax Assessment Act 1936* s 161.

24 *Income Tax Assessment Act 1936* s 6(1); *Income Tax Assessment Act 1997* ss 5-5(5)-(7).

25 *Taxation Administration Act 1953* Sch 1 Pt 2-10.

26 *Taxation Administration Act 1953* Pt IIB Div 3, Sch 1 s 6-10, Divs 12-14, 18.

- 1.26 Dates for the lodgment of tax returns and activity statements as well as the payment of liabilities vary according to the type of taxpayer entity and their previous lodgment compliance.²⁷ The ATO, however, has discretion to alter the date on which the tax is payable by granting an extension of time or allowing payment to be made by instalments.²⁸ A General Interest Charge (GIC) accrues from the due date of the original payment, which is generally 21 days after lodgment is required or an assessment is issued,²⁹ until the tax liability is paid. The ATO retains discretion to remit any or all of the interest.³⁰
- 1.27 Any tax liability that remains unpaid after it has become due and payable is a 'debt' to the Commonwealth of Australia and recovered in any court of competent jurisdiction by either the Commissioner of Taxation (Commissioner) or a Deputy Commissioner.³¹
- 1.28 Certain submissions to this review made comments that some taxpayers may not comply with their lodgment requirements in an effort to avoid or delay tax liabilities being raised and tax becoming payable. In addition to GIC, Failure to Lodge (FTL) penalties will be charged for each 28 day period (or part thereof) up to a maximum amount (currently between \$850 and \$4,250 depending on the size of the taxpayer).³² In some cases, the ATO may also issue a default assessment where lodgment has not occurred.³³ Where the ATO issues a default assessment, administrative penalties between 75 per cent and 95 per cent of the tax-related liability will be applied depending on the taxpayer's compliance history.³⁴
- 1.29 The IGT has previously reviewed the ATO's approach to the non-lodgment of individual income tax returns in 2009 and made recommendations aimed at improving compliance with lodgment obligations. Whilst the ATO's management of non-lodgment is beyond the scope of this review, it is important to keep in mind that non-lodgment has bearing on the level of debt in the revenue system and may be an important part of any revenue authority's strategies for addressing tax debts.

27 ATO, *Tax Returns by Client Type* (1 July 2014) <<https://www.ato.gov.au>>.

28 *Taxation Administration Regulations 1976* reg 18(3); *Taxation Administration Act 1953* sch 1 ss 255-10, 255-15.

29 For example, ss 5-5 and 5-15 of the *Income Tax Assessment Act 1997*; a full list of due and payable dates is summarised in section 250-10 of Schedule 1 to the *Taxation Administration Act 1953*.

30 *Income Tax Assessment Act 1997* ss 5-15; *Taxation Administration Act 1953* s 8AAG and sch 1 s 255-10.

31 Tax-related reliability means a pecuniary liability to the Commonwealth arising directly under a taxation law, including a liability which is not yet due and payable: *Taxation Administration Act 1953* sch 1 s 255-1, s 255-5(2).

32 The quantum of the penalty depends on the size of the taxpayer and the length of time lodgment was not made: *Taxation Administration Act 1953* ss 286-75, 286-80.

33 *Income Tax Assessment Act 1936* s 167.

34 ATO, *Default Assessment for Overdue Lodgment Obligations* (July 2014) <<https://www.ato.gov.au>>.

REPORTING TAX DEBTS

- 1.30 The ATO publicly reports on the levels of tax debt as at the end of each financial year in its Annual Reports. The Annual Reports account for tax debt using three main categories which are:
- collectable debt – when liabilities are due and payable and not subject to dispute or the taxpayer is not subject to some form of insolvency administration;³⁵
 - disputed debt – when liabilities are due and payable but are the subject of a dispute under Part IVC of the *Tax Administration Act 1953*, for example, an objection, tribunal review or a court appeal;³⁶ and
 - insolvent debt – when liabilities are due and payable but the taxpayer is subject to some form of insolvency administration.³⁷
- 1.31 The ATO also reports specifically on debts which are ‘written off’³⁸ being those which are determined to be:
- irrecoverable at law (that is, bankruptcy or wind up); and
 - uneconomic to pursue.³⁹
- 1.32 For insolvent amounts and those which are written off, the ATO makes provision for bad and doubtful debts, according to its Annual Report. An estimate of the amount which is not expected to be recovered is also provided in the ATO’s Annual Reports. The provision for bad and doubtful debts is offset against total gross taxation receivables which provide an estimate of the collectable amounts (net total taxation receivables).⁴⁰
- 1.33 Debts are automatically characterised as collectable when the date for payment in the ATO’s systems has passed. The ATO manually changes the characterisation where the taxpayer notifies the ATO of a dispute or insolvency and the relevant record is inputted against the taxpayer’s account.⁴¹
- 1.34 Internal ATO reports, known as ‘Debt Knowledge Updates’ that report and analyse the level of debt holdings are sourced from ATO systems and provided to senior officers on a monthly basis. These reports are used to monitor the ATO’s performance against strategic objectives.

35 Commissioner of Taxation, *Annual Report 2013-14* (2014) p 251.

36 ATO, ‘Collectable vs Impeded Debt’ (Internal ATO document, 2011).

37 Ibid; Commissioner of Taxation ‘Annual Report 2013-14’, above n 35, p 50.

38 Debts which are uneconomic to pursue or irrecoverable at law and written off may be re-raised at a later date should information subsequently become available which indicates that recoverability action may now be viable: Commissioner of Taxation ‘Annual Report 2013-14’, above n 35, p 193.

39 Commissioner of Taxation ‘Annual Report 2013-14’, above n 35, pp 50, 193.

40 Ibid p 88, 226.

41 ATO, ‘Collectable vs Impeded Debt’, above n 36.

COMPOSITION OF TOTAL DEBT MANAGED BY THE ATO

- 1.35 Internal ATO reports state that approximately 89 per cent of taxes are paid on time which equates to 75 per cent of taxpayers. Of the amounts which are not paid on time, 97 per cent are paid within 12 months, corresponding to 92 per cent of taxpayers.⁴²
- 1.36 However, the ATO acknowledges that it is facing challenges with managing tax debts. It has not met its deliverables or its Key Performance Indicators (KPI) for collecting and managing tax debts in the last two financial years as shown in its 2013–14 Annual Report, reproduced below.⁴³

Figure 1.4: Recent ATO debt targets

Collect and manage debt

2011–12	2012–13	2013–14
✓	✗	✗

The value of collectable debt at the end of June 2014 was almost \$19.5 billion, an increase of 10.0% compared to the end of June 2013. This was despite collections attributable to our debt collection actions increasing by 4.8% in 2013–14 compared to 2012–13.

Challenges in the economy are continuing to affect some taxpayers' ability to pay. In 2013–14, the inflow of new debt continued to outpace improvements in our debt management performance, resulting in an increase in collectable debt holdings.

ATO collectable debt as a percentage of collections in the context of the current economic environment

2011–12	2012–13	2013–14
✓	✗	✗

The increase in collectable debt as a percentage of collections reflects the 10.0% year-on-year increase in collectable debt, with net tax collections increasing only 3.2% over the year.

Small businesses accounted for 58.6% of the year-on-year increase, with small-to-medium enterprises accounting for virtually all of the balance. Income tax accounted for 75.3% of the year-on-year increase.

The ongoing impact of the economic environment on some taxpayers' ability to pay was the key underlying driver of the increase in collectable debt.

Commissioner of Taxation.

Gross Domestic Product and composition of total tax debt

- 1.37 It is commonly accepted that the level of tax debt may be as a result of underlying economic activity.⁴⁴ Economic activity may be measured using Gross Domestic Product (GDP). The following shows the total amount of tax debt as a proportion of GDP from the 2010–11 to 2013–14 financial years.

⁴² ATO, 'Debt Strategy 2014-18' (Internal ATO document, undated).

⁴³ Commissioner of Taxation 'Annual Report 2013-14', above n 35, pp 14-17.

⁴⁴ Commissioner of Taxation 'Annual Report 2013-14', above n 35, p 44.

Table 1.1: Amount of total tax debt managed by the ATO as a proportion of GDP over 2010–11 to 2013–14

	2010–11 (in \$m)	2011–12 (in \$m)	2012–13 (in \$m)	2013–14 (in \$m)
Total debt	26,859	30,859	32,214	35,344
Percentage change from prior year (debt)	–	14.89%	4.39%	9.72%
GDP^(a)	1,430,682	1,483,295	1,520,622	1,558,398
Percentage change from prior year (GDP)	–	3.68%	2.52%	2.48%
Percentage of GDP	1.88%	2.08%	2.12%	2.27%

Source: ATO data; Australian Bureau of Statistics, S 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates.

(a) GDP = Gross domestic product: chain volume measures. GDP has been calculated by totalling the September, December, March and June quarters for each financial year.

Note: Figures and percentages are rounded.

- 1.38 Table 1.1 shows, whilst GDP has increased over time, total tax debts have also increased but at a faster rate such that the percentage of debt as a proportion of GDP has risen year-on-year from 1.88 per cent in 2010–11 to 2.27 per cent in 2013–14.
- 1.39 The total amount of tax debt managed by the ATO from the 2010–11 to 2013–14 financial years by type of debt is set out in the table below.

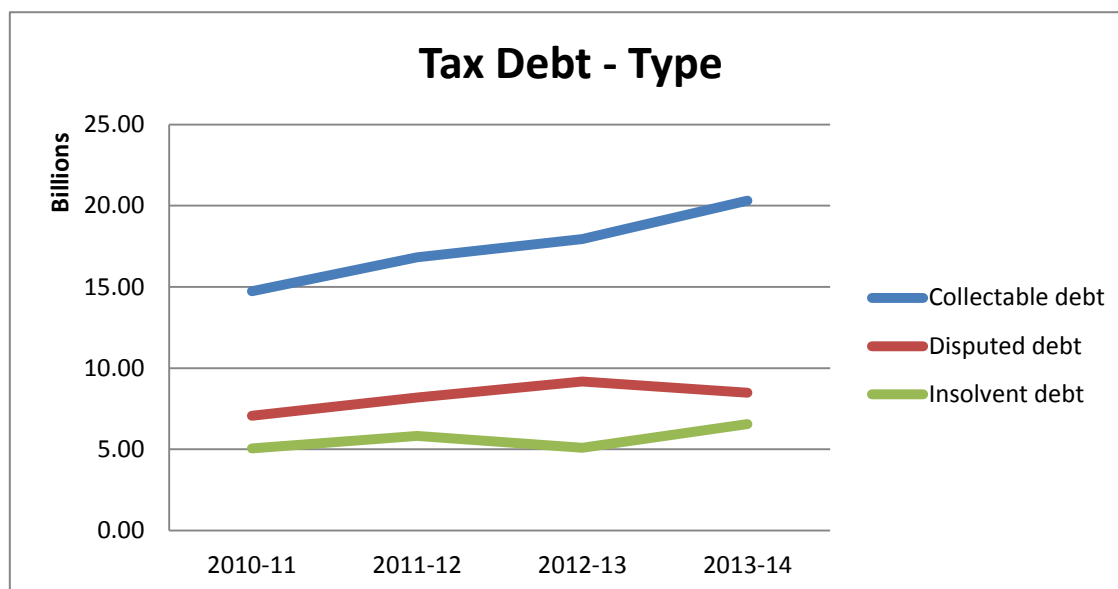
Table 1.2: Composition of total tax debt managed by the ATO over 2010–11 to 2013–14

Type of debt	2010–11 (in \$m)	% of total	2011–12 (in \$m)	% of total	2012–13 (in \$m)	% of total	2013–14 (in \$m)	% of total
Collectable	14,736	55%	16,833	54%	17,943	56%	20,316	57%
Disputed	7,064	26%	8,200	27%	9,180	28%	8,481	24%
Insolvent	5,059	19%	5,825	19%	5,091	16%	6,547	19%
Total	26,859	100%	30,858	100%	32,214	100%	35,344	100%

Source: IGT analysis of ATO data.

Note: Figures and percentages are rounded.

- 1.40 Table 1.2 shows that over this four year period, collectable debt has comprised the majority of total tax debt (55–57 per cent), followed by disputed debt (26–29 per cent) and insolvent debt (16–19 per cent). The percentage of collectable debt has slightly increased as a proportion of total debt from the 2010–11 financial year to the 2013–14 financial year from 55 per cent to 57 per cent respectively.
- 1.41 The proportion of disputed debt rose from 26 per cent to 29 per cent over the first three years and then fell by 5 per cent to 24 per cent in 2013–14.
- 1.42 Lastly, the proportion of insolvent debt has stayed constant at 19 per cent, with the exception of the 2012–13 year when the percentage dropped to 16 per cent of total debts.
- 1.43 The graph below in Figure 1.5 uses the data in Table 1.2 to visually represent the above movements in the levels of collectable, disputed and insolvent debts respectively.

Figure 1.5: Composition and trend in total tax debts over 2010–11 to 2013–14

Source: IGT analysis of ATO data.

Net tax collections and collectable debt

- 1.44 A key performance indicator for many revenue authorities is the ratio of collectable debt to net tax collections (which excludes any transfer payments).⁴⁵ The following table sets out the ratio of collectable debt to net tax collections from the 2010–11 to 2013–14 financial years.

Table 1.3: Ratio of collectable debt to net tax collections over 2010–11 to 2013–14

Type	2010–11	2011–12	2012–13	2013–14
Collectable Debt (\$B)	14.1	16.6	17.7	19.5
Net tax collections (\$B)	273.0	301.0	311.8	321.6
Ratio	5.2%	5.5%	5.7%	6.1%

Source: ATO communication to the IGT 29/1/15

- 1.45 The above table shows that whilst net tax collections have increased, so has collectable debt but at an increased rate such that the ratio of collectable debt to net tax collections has increased from 5.2 per cent at 30 June 2011 to 6.1 per cent at 30 June 2014.⁴⁶

Composition of collectable debt

- 1.46 As mentioned earlier, collectable debt is the largest proportion of total tax debt. It is broken down by market segment in the following table for the financial years 2010–11 to 2013–14.

⁴⁵ OECD, *Working Smarter in Tax Debt Management* (2014) pp 80–81.

⁴⁶ Commissioner of Taxation 'Annual Report 2013–14', above n 35, p 50.

Table 1.4: Composition of total collectable debts by market segment over 2010–11 to 2013–14

Market Segment	2010–11 (in \$m)	% of total	2011–12 (in \$m)	% of total	2012–13 (in \$m)	% of total	2013–14 (in \$m)	% of total
Individuals	2,450	16%	2,914	17%	2,854	16%	3,150	16%
Small business	9,046	60%	10,090	59%	10,966	60%	12,459	60%
Large business	265	0% (0.02%)	530	0% (0.03%)	575	0% (0.03%)	245	0% (0.01%)
Other	3,205	23%	4,046	24%	4,334	24%	4,928	24%
Total	14,967	100%	17,049	100%	18,154	100%	20,538	100%

Source: IGT analysis of ATO data.

Note 1: Figures and percentages are rounded.

Note 2: 'Other' category, includes government, medium business and not for profit entities.

- 1.47 As evidenced by the table above, the main contributor to collectable debt is the small business market segment. Since 2010, the amount of small business collectable debt has increased by approximately \$1 billion each year over 2010–11 to 2012–13 and by more than \$2 billion in 2013–14. On the other hand, large business forms a negligible amount of collectable debt. The relative proportions of the different market segments' contributions to collectable debt have remained fairly constant over the 2010–11 to 2013–14 financial year period.
- 1.48 Small business collectable debt, approximately 60 per cent of total collectable debt, may be further broken down by turnover range. The following table shows the breakdown for the 2010–11 to 2013–14 financial years.

Table 1.5: Composition of total small business collectable debt by turnover range over 2010–11 to 2013–14

Small Business	2010–11 (in \$m)	% of total	2011–12 (in \$m)	% of total	2012–13 (in \$m)	% of total	2013–14 (in \$m)	% of total
\$0–\$500K	6,815	75%	7,626	76%	8,228	75%	9,169	74%
\$500K–\$1M	1,155	13%	1,320	13%	1,453	13%	1,516	12%
\$1M–\$2M	1,066	12%	1,137	11%	1,277	12%	1,774	14%
\$2M or more	11	0%	7	0%	8	0%	1	0%
Total	9,046	100%	10,090	100%	10,966	100%	12,459	100%

Source: IGT analysis of ATO data.

Note: Figures and percentages are rounded.

- 1.49 The table above shows that approximately 75 per cent of small business collectable debt is in the \$0 to \$500,000 turnover range. The ATO defines businesses with this turnover range as micro businesses. Over the four year period, the proportion of micro business collectable debt has increased by one percentage point in 2011–12 and then decreased by a percentage point each year thereafter.

- 1.50 The proportion of small business collectable debt within the \$500,000 to \$1 million turnover range has stayed at 13 per cent from 2010–11 to 2012–13 and then decreased by one percentage point in 2013–14. The \$1 million to \$2 million turnover range has varied between 11 per cent and 14 per cent over the four years and there was no noticeable change in the \$2 million or more turnover range due to the comparatively smaller amounts of collectable debt in this segment.
- 1.51 Micro business collectable debt, being the largest proportion of small business collectable debt, requires further analysis. The ATO's systems facilitate such analysis by the age of the debt.
- 1.52 The table below segments micro businesses collectable debt by age for the 2012–13 financial year. The table also distinguishes between income tax and other debt types.

Table 1.6: Composition of total micro business collectable debt by age and debt type in 2012–13

Micro business	0–2 mths old (in \$m)	% of total	2–6 mths old (in \$m)	% of total	>6mth old (in \$m)	% of total	Total debt	% of total
Income tax	1,417	10%	1,849	13%	1,858	13%	5,124	37%
Other	1,922	14%	3,454	25%	3,526	25%	8,902	63%
Total	3,339	24%	5,303	38%	5,384	38%	14,026	100%

Source: IGT analysis of ATO data.

Note: Figures are rounded and may not align to Table 1.5 due to how the ATO categorises micro businesses.

- 1.53 Two observations may be made in relation to Table 1.6 above. First, the 'other' debts comprise the largest amounts of micro business collectable debts (63 per cent). Secondly, the majority of both income tax and other debts are aged less than 6 months (62 per cent).
- 1.54 Table 1.7 below specifies the total amount of individual taxpayer collectable debt by age bands for the 2012–13 financial year.

Table 1.7: Composition of total individual collectable debt by age in 2012–13

AGE	Individuals	
	Quantum (\$)	% of total
0 – 2 months	897,368,280.56	30.28%
2 – 6 months	437,806,973.78	14.78%
6 months – 1 Year	430,910,677.92	14.54%
1 – 2 years	478,738,145.25	16.16%
2 + years	718,316,921.03	24.24%
Total	2,963,140,998.54	100.00%

Source: IGT analysis of ATO data.

Note: Total individual collectable debt may not align to Table 1.4 due to the data sourced from different ATO systems.

- 1.55 The table above shows that a large proportion (30 per cent) of individual collectable debt is less than two months old after which it remains fairly constant (14 to 16 per cent) until it spikes again in the more than two years old range (24 per cent). Compared to Table 1.6 above, there is a greater proportion of individual collectable debt that is aged greater than 6 months (55 per cent).

Composition of total insolvent debt

- 1.56 The table below shows the amount of insolvency debt from the 2010–11 to 2013–14 financial years, stratified by market segment.

Table 1.8: Composition of total insolvent tax debt by market segment over 2010–11 to 2013–14

Market Segment	2010–11 (in \$m)	% of total	2011–12 (in \$m)	% of total	2012–13 (in \$m)	% of total	2013–14 (in \$m)	% of total
Individuals	488	9%	579	10%	391	7%	430	6%
Small business	3,506	67%	4,006	66%	3,466	65%	4,321	64%
Large business	313	6%	57	1%	106	2%	62	1%
Other	923	18%	1,416	23%	1,385	26%	1,987	29%
Total	5,230	100%	6,058	100%	5,348	100%	6,791	100%

Source: IGT analysis of ATO data.

Note: Figures and percentages are rounded.

- 1.57 Table 1.8 above shows that small businesses account for 64–67 per cent of insolvent debt. It is also noteworthy that, generally, there is a small decline in insolvent debt for all market segments, as a percentage of the total, except for the ‘other’ category which represents government, medium businesses and not-for-profit entities.
- 1.58 The table below shows the small business insolvency debt from the 2010–11 to 2013–14 financial years broken up by turnover range.

Table 1.9: Composition of total insolvent small business tax debt by turnover range over 2010–11 to 2013–14

Small Business	2010–11 (in \$m)	%	2011–12 (in \$m)	%	2012–13 (in \$m)	%	2013–14 (in \$m)	%
\$0–\$500K	2,842	81%	3,143	78%	2,568	74%	2,540	59%
\$500K–\$1M	362	10%	412	10%	422	12%	1,228	28%
\$1M–\$2M	298	8%	449	11%	468	14%	552	13%
\$2M or more	4	0%	3	0%	7	0%	1	0%
Total	3,506	100%	4,006	100%	3,466	100%	4,321	100%

Source: IGT analysis of ATO data.

- 1.59 The table above shows that the micro business market segment has the largest amount of insolvency debt compared to other small business turnover segments. The micro business proportion of total insolvency debt has steadily decreased from approximately 81 per cent in 2010–11, to approximately 78 per cent, 74 per cent and 59 per cent in 2011–12, 2012–13 and 2013–14 respectively. However, over time, it appears that small businesses with turnover between \$500,000 and \$1 million almost tripled their amounts of insolvency debt from \$422 million in 2012–13 to \$1.228 billion in 2013–14. Insolvent debts for small businesses with turnover above \$2 million have also varied over this time but continue to represent a negligible amount of total insolvency debt.

RECOVERY OF TAX LIABILITIES

1.60 The Commissioner has a number of methods to recover debts which are:

- payment by instalments (payment arrangements);
- garnishee notices;
- DPNs;
- freezing orders (also known as Mareva injunctions);
- DPOs;
- security;
- offsetting credits with debits; and
- insolvency action.⁴⁷

1.61 The ATO takes a different approach where debts are disputed. Each of these mechanisms and the disputed debt approach are described in more detail in the sections below.

Payment arrangements

1.62 The Commissioner may accept the payment of the debt by way of instalments (payment arrangements). The Commissioner is not obliged to accept payment arrangements and makes such decisions based on risk.⁴⁸ As part of this risk analysis, if the prospects of recovery in the longer term would be diminished or the revenue would be disadvantaged, payment arrangements will not be accepted.⁴⁹

1.63 In deciding whether to accept a payment arrangement, the ATO expects staff to consider and apply the practice statement where relevant.⁵⁰ The main considerations outlined in the practice statement are the:

- information provided by the taxpayer and any other information;
- circumstances that led to the inability to pay, the taxpayer's current financial position and actions taken to rearrange finances or borrow to meet the debt;
- stage that any legal recovery action has reached and the grounds offered by the taxpayer to justify a request that further legal action be deferred as well as alternative recovery options that may result in quicker payment;

⁴⁷ Insolvency action includes legal action, up to and including the liquidation of companies or the bankruptcy of an individual, such as by way of summons, judgment, bankruptcy notice, creditor's petition, s 459E notices and wind up summons.

⁴⁸ ATO, *General Debt Collection Powers and Principles*, PS LA 2011/14, 3 July 2014, para [56].

⁴⁹ Ibid, para [63].

⁵⁰ Ibid, para [61].

- taxpayers' ability to pay the debt without seriously impacting the taxpayer's ability to meet other obligations, including the solvency of the taxpayer and arrangements made with other creditors to pay debts;
 - risk to the revenue by accepting the payment arrangement and whether that risk could be overcome by seeking some form of security;
 - taxpayers' compliance with other tax obligations or commitments (for example, lodgment) and the history of the taxpayer's prior dealings with the ATO; and
 - willingness of the taxpayer to enter into direct debit arrangements if possible as well other conditions under which the ATO will agree to a payment arrangement.
- 1.64 The ATO may conduct a review of the taxpayer's viability and capacity to pay using its support tools and calculators, such as the Business Viability Assessment Tool (BVAT) and an Independent Viability Assessment (IVA) which are described in more detail in a later section. Similarly, the ATO also has a tool to help determine an individual's capacity to pay—called the Debt Serviceability Tool (DST). The BVAT, independent viability assessments and DST are further described later in this chapter.
- 1.65 The ATO has advised that any assessment of the taxpayer's viability and capacity to pay, by the above support tools, is not conclusive by itself and is only intended to support officers in making decisions. For example, such assessments may be considered in combination with other information, such as future cash projections. Where it is determined that the taxpayer is not viable or does not have capacity to pay, payment arrangements will not be accepted by the ATO and formal recovery action may commence.⁵¹
- 1.66 As part of the payment arrangement process, taxpayers are requested to make an upfront payment according to their capacity.⁵² The ATO generally encourages such payments to be at least 20 per cent of the outstanding debt. However, a payment of up to 50 per cent may be required depending on the level of risk or where debts are disputed.⁵³
- 1.67 The ATO also acknowledges that there will be instances where the timeframe to pay may extend over more than one financial year depending on a range of factors, such as the capacity to pay, the size of the debt and the likely costs of alternative recovery activity. In these circumstances, taxpayers may be required to provide security where there are concerns about their solvency or their ability to meet the payment terms proposed.⁵⁴

⁵¹ ATO, Communication to the IGT, 8 January 2015.

⁵² ATO, 'General Debt Collection Powers and Principles' above n 48, para [60].

⁵³ ATO, 'Debt Engagement – Guiding Principles' (Internal ATO document, undated); ATO, 'DRN Company Matrix' (Internal ATO document, undated); ATO, 'DRN Individual Matrix' (Internal ATO document, undated).

⁵⁴ ATO, 'General Debt Collection Powers and Principles' above n 48, para [60], paras [63]–[64].

- 1.68 Where a significant change in the taxpayer's circumstances occurs, the ATO may, having regard to any representations that have been made by the taxpayer, vary the terms of the arrangement or proceed to recover the debt in full.⁵⁵
- 1.69 A taxpayer may contact the ATO to enter into a payment arrangement. Decisions to accept or reject payment arrangements are made by ATO staff within the scope of pre-determined authorisations. These are set out below.

Table 1.10: ATO staff authorisations to accept and refuse payment arrangements

Officer level	Cadet	APS1	APS1	APS2	APS3	APS4	APS5	APS6	EL1
Accept arrangements									
Max period	24mths	24mths	12mths	24mths	24mths	36mths	36mths	∞	∞
Max amount	\$500k	\$25k	\$50k	\$150k	\$500k	\$1.5m	\$2.5m	\$5m	∞
Refuse arrangements									
Max period	∞	∞	∞	∞	∞	∞	∞	∞	∞
Max amount	\$500k	\$50k	\$150k	\$500k	\$1.5m	\$2.5m	\$5m	∞	∞

Source: ATO, Taxation Authorisations Guidelines (Internal ATO document, November 2014).

Garnishee notices

- 1.70 Where tax liabilities are not paid by the due date, the ATO will use various methods to recover the debt that is considered the most appropriate for dealing with the tax debtor.⁵⁶ One method is that the ATO may collect tax from any person owing money to the taxpayer, including liquidators, receivers, trade debtors, bank accounts and certain agents.⁵⁷ Where a third party owes money to the taxpayer, the ATO may at any time, by notice in writing (garnishee notice) to both the taxpayer and third party, require the third party to pay to the ATO the monies owing (up to the amount of tax due) in order to meet the tax debt.⁵⁸
- 1.71 The ATO states that, generally, garnishee notices are issued to taxpayers who have failed to engage with the ATO to satisfy their debts, such as situations where:
- taxpayers have not kept their commitment to provide additional information;
 - taxpayers have not responded to the Notice of Intended Legal Action (NILA) or a Firmer Action Warning (FAW) letter; or
 - a suitable payment plan was unable to be negotiated.⁵⁹

⁵⁵ Ibid, para [69].

⁵⁶ ATO, *Enforcement Measures used for the Collection and Recovery of Tax-Related Liabilities and Other Amounts*, PS LA 2011/18, July 2014, paras [14]-[17].

⁵⁷ *Taxation Administration 1953* Sch 1 ss 260-5, 260-45(2), 260-75(2), 260-105(2).

⁵⁸ *Taxation Administration 1953* Sch 1 s 260-5.

⁵⁹ ATO, 'Debt - Issue Point in Time (PIT) garnishee notice' (Internal ATO document, July 2014).

- 1.72 In determining whether to issue a garnishee notice, the ATO directs officers to have regard to:
- particular circumstances of the taxpayer, such as their financial position (for example, the taxpayer is in receivership, a lower income earner or on Centrelink benefits)⁶⁰ and the steps taken to make payment;
 - the extent of any other debts owed by the taxpayer;
 - whether the revenue is at risk due to the actions of the taxpayer, such as paying other creditors in preference to the ATO; and
 - the impact of issuing a notice on a taxpayer's ability to provide for their family or to maintain the viability of a business.⁶¹
- 1.73 The ATO expects its staff to consider the case history and take a 'whole of client' approach to verify the decision to issue a garnishee notice.⁶²
- 1.74 The ATO considers that garnishee notices to a third party are often an efficient and cost effective way of obtaining payments of outstanding tax debts and may be used in a number of circumstances.⁶³
- 1.75 The ATO directs its staff to not issue garnishee notices in a range of circumstances including where a debt is disputed, recovery action is otherwise deferred, taxpayers have an active complaint or the debt is referred to an external debt collection agency.⁶⁴ However, in high risk cases, the ATO may depart from these rules for strategic reasons.⁶⁵
- 1.76 The ATO generally requires staff to ensure taxpayers are fully informed of intended firmer recovery action. Taxpayers are considered to have been warned of potential garnishee action after receiving a warning letter, such as FAW letters or 'notices of intended legal action'.⁶⁶ However, in higher risk cases where there are 'compelling strategic reasons',⁶⁷ the ATO may permit the issuing of garnishee notices without warning:

The notice can be used as soon as an assessment is validly served, and even before the due date for payment has passed. Where a garnishee source has been identified, but the likely financial return is considered insignificant relative to the quantum of the debt, a garnishee is still considered a highly-effective recovery tool to encourage engagement.

60 ATO, *Insolvency - Collection, Recovery and Enforcement Issues for Entities under External Administration*, PS LA 2011/16, 4 November 2014; ATO, 'Issue Standard Garnishee' (Internal ATO document, November 2014); ATO, 'Enforcement Measures', above n 56, paras [108]-[123].

61 ATO, 'Enforcement Measures', above n 56, para [102].

62 ATO, 'PIT garnishee notice' above n 59.

63 ATO, 'Significant Debt Management: Guidelines for Effective Case Management' (Internal ATO document, November 2014) pp 13-14.

64 ATO, 'PIT garnishee notice' above n 59.

65 Ibid.

66 ATO, 'Debt Reference Manual' (Internal ATO document, September 2014) [Garnishee notices].

67 Such as 'serious tax evasion or fraud': ATO, Communication to the IGT, 6 May 2015.

The Commissioner will consider any reasonable request from a taxpayer to either withdraw or vary a garnishee notice, preferably once the taxpayer makes suitable alternative arrangements for payment – which makes garnishee notices effective in encouraging engagement and ongoing compliance.⁶⁸

1.77 Standard garnishee notices may be used for fixed amounts, whereas point in time notices may be used to secure a proportion of funds.⁶⁹ For point in time garnishee notices, ATO staff are directed to minimize the impact on employees or the taxpayer's ability to pay everyday expenses, such as food, water and other living expenses. The Debt Reference Manual (DR Manual) notes that it is generally inappropriate, other than in exceptional circumstances, to garnish all of the money in the taxpayer's accounts or issue a garnishee of 100 per cent of money owed by trade debtors. The DR Manual outlines a range of situations and amounts for which point in time garnishee notices are commonly issued, including those to:

- financial institutions which are generally for 30 per cent of available money (the ATO expects financial institutions to check all accounts held in a taxpayer's name) but the proportions are decided on a case-by-case basis;
- trading accounts which are for amounts being the lesser of 30 per cent of the outstanding debt or 30 per cent of gross sales less gross salary and wages;
- trade debtors which for the lesser of 30 per cent of the outstanding debt or 30 per cent of the trade debt; and
- employers which are for varying amounts depending on taxpayers' circumstances, for example, if the taxpayer is married or with dependents, 20 per cent of their gross wage.⁷⁰

1.78 The ATO may also exercise 'strategic discretion' as to the debt amount to be included and the rate to be paid.⁷¹

1.79 The ATO has tiered authorisations for staff to issue garnishee notices depending on the amount to be garnished. These are shown in the table below.

Table 1.11: ATO staff authorisations to issue garnishee notices to third parties

Officer level	APS1	APS2	APS3	APS4	APS5	APS6	EL1	EL2	SES
Amount	N/A	\$50K	\$250K	\$1mil	∞	∞	∞	∞	∞

Source: ATO, 'Taxation Authorisations Guidelines' (Internal ATO document, November 2014).

68 ATO, 'Significant Debt Management', above n 63, p 14.

69 Ibid, pp 14-15.

70 ATO, 'Debt Reference Manual', above n 66, [Garnishee notices].

71 ATO, 'Significant Debt Management', above n 63.

- 1.80 There may be occasions where it is necessary for the ATO to either amend, reduce, revoke, vary or withdraw a garnishee notice. For example, where the debts for which garnishee notices were issued have either increased or decreased, the notice was issued in relation to funds that are not the property of the taxpayer (for example, amounts held on trust) or amounts obtained due to bank error. The ATO procedures direct officers to consider any reasonable request from a debtor to change or withdraw the requirements of a garnishee notice if the debtor makes alternative and satisfactory arrangements for payment of the debt. Such a decision must be made in consultation with a coaching officer.⁷²

Director Penalty Notices

- 1.81 Pursuant to section 269–20 of Schedule 1 to the *Taxation Administration Act 1953* (TAA 1953), company directors may incur a personal liability for unpaid PAYG Withholding and Superannuation Guarantee Charge (SGC) liabilities of their company, including estimates of those liabilities. Where such a penalty is incurred by a director, the Commissioner will issue a DPN.⁷³
- 1.82 The ATO must not commence recovery proceedings until 21 days after the director is given a DPN.⁷⁴ Any recovered amounts will trigger a parallel reduction of the company's liability. ATO staff at or above the APS 3 level have authorisation to issue DPNs.⁷⁵
- 1.83 There are several variants of DPNs. For example, in cases where the liability was not reported within three months of the due date, it will continue to be owed by the director, even where the company is subsequently placed into voluntary administration or liquidation. These 'locked-down' penalties will be represented on a separate notice for clarity.⁷⁶
- 1.84 Appendix 2 of this report contains flow charts which describe the process for issuing DPNs with respect to PAYG Withholding, Superannuation Guarantee Charge (SGC) and for new directors. Figure A2.2 describes the process for PAYG Withholding. Briefly, the process begins with a company registering for PAYG Withholding with the ATO. Once the company starts to pay wages, it is required to lodge periodic activity statements. If the activity statement is lodged by the due date but payment is not made or if lodgment occurs within three months of the due date, the ATO will attempt to contact the company. If the debt remains outstanding, other collection actions will be considered, such as garnishee action. If the company does not engage with the ATO after such action, the ATO will issue a standard DPN. Where lodgment is not made within three months of the due date, the ATO will continue to attempt contact. Where contact is unsuccessful, the ATO will issue a 'lockdown' DPN.

72 ATO, 'Debt Reference Manual', above n 66, [Garnishee notices]; ATO, 'Amend, Reduce, Revoke, Vary or Withdraw a Garnishee Notice' (Internal ATO document, July 2014).

73 *Taxation Administration Act 1953* sch 1 s 269-25; ATO, 'Enforcement Measures', above n 56, para [47].

74 ATO, 'Enforcement Measures', above n 56, para [47].

75 ATO, 'Taxation Authorisation Guidelines' (Internal ATO document, November 2014) para [5.4.9].

76 ATO, 'Enforcement Measures', above n 56, paras [52]-[53].

- 1.85 Figure A2.3 describes a similar process with respect to superannuation guarantee obligations. However, at the outset, the ATO considers whether payment has been made to a superannuation fund by the due date. If not, then a similar process to DPNs being issued with respect to PAYG Withholding occurs.
- 1.86 Figure A2.4 describes the process in relation to new company directors. If lodgments are made by the due date or within three months of the appointment of a new director, but not paid within 30 days of the director's appointment, the ATO will issue a standard DPN. If lodgments are not made within three months of the director's appointment, a 'lockdown' DPN will be issued.
- 1.87 Section 269–35 of Schedule 1 to the TAA 1953 sets out limited statutory defences to a DPN which are:
- if, because of illness or some other good reason, it would have been unreasonable to expect the director to take part (and in fact they did not take part) in the management of the company at any time when a director of the company and the directors were under an obligation to cause the company to meet its payment obligation, or
 - the director took all reasonable steps to ensure the directors caused one of these three things to happen (or no such steps were available):
 - the company to comply with its obligation to pay,
 - an administrator of the company to be appointed, or
 - the company to begin to be wound up.

In determining what are reasonable steps that a director could have taken, regard must be had to when and for how long the person was a director and took part in the management of the company, and all other relevant circumstances.⁷⁷

- 1.88 In addition to the above defences, a director is not liable for a penalty with respect to unpaid superannuation guarantee where it has taken reasonable care and adopted a position which is based on a reasonably arguable interpretation of the relevant legislation. There is no similar defence in relation to PAYG Withholding.⁷⁸

Freezing orders

- 1.89 A freezing order (or Mareva injunction)⁷⁹ is a court order which prevents a person from accessing and dealing with their money or assets. A court may make a freezing order 'for the purpose of preventing the frustration or inhibition of the court's process by seeking to meet a danger that a judgment or prospective judgment of the court will be wholly or partly unsatisfied'.⁸⁰

⁷⁷ Ibid, para [54]-[55].

⁷⁸ Ibid, para [62]-[63].

⁷⁹ *Mareva Compania Naviera SA v. International Bulkcarriers SA [the Mareva]* [1975] 2 Lloyd's Rep 509.

⁸⁰ ATO, 'Enforcement Measures', above n 56, para [169]-[170].

- 1.90 To justify a freezing order, the court must be of the view that there is a real and not merely fanciful risk:

that, in the absence of an injunction any assets wherever located which the respondent may have, will be dissipated or dealt with in some fashion such that the applicant will not be able to have the judgment satisfied.⁸¹

- 1.91 Accordingly, the ATO will generally apply to the court for a freezing order where the ATO believes there is an unacceptable risk that the taxpayer will dissipate assets so that the debts will remain unpaid.⁸²

- 1.92 The ATO's risk assessment processes requires a number of elements to be addressed in relation to the court's rules as well as common law,⁸³ which include:

- non-payment of the debt by the due date;
- the requirement to avoid injustice to the taxpayer by making full disclosure, including of matters that may be prejudicial to the ATO's case where ex parte application is made;
- evidence of the existence of assets owned by the taxpayer within the jurisdiction; and
- evidence for believing that there is a risk of the assets being moved from the jurisdiction or dissipated so that the debts will remain unpaid, including where assets are held by third parties but the taxpayer exercises control over the property or where property was transferred through sham transactions or fraudulent conveyances.⁸⁴

- 1.93 As freezing orders may have serious consequences for a taxpayer, it may lead to substantial claims being made against the Commissioner where it is found to be unjustified. The Commissioner is ordinarily required to give an undertaking as to damages, which may be supported by a bond or other security. Accordingly, the ATO aims to ensure that the freezing order is not too wide, catching unnecessary assets or extending to assets greater in value than are necessary to meet the claim.

Departure Prohibition Orders

- 1.94 A DPO is an administrative instrument issued by the Commissioner which aims to ensure that Australian tax liabilities are paid by preventing a person from leaving Australia for a foreign country.

⁸¹ Ibid, para [175]-[178].

⁸² Ibid, para [171].

⁸³ *Third Chandris Shipping Corp. v. Unimarine S.A.* (1979) QB 645, 668.

⁸⁴ ATO, 'Enforcement Measures', above n 56, para [179].

- 1.95 Unless authorised by a Departure Authorisation Certificate (DAC), a taxpayer who is aware of a DPO must not depart for a foreign country notwithstanding any intention to return to Australia.⁸⁵ A DAC may be provided where a taxpayer is expected to return to Australia within an appropriate timeframe. Where the ATO is not satisfied in relation to the latter, it may still issue a DAC where the taxpayer has given satisfactory security, there are humanitarian grounds or it is otherwise detrimental to the interests of Australia.⁸⁶ Any security provided by the taxpayer does not necessarily have to be commensurate with the size of the tax liability. In such instances, the ATO will consider circumstances, such as the risk of the taxpayer not returning to Australia, who owns the assets offered as security, the impact on the forfeiture of security on the taxpayer, the size of the security relative to the tax liability and other assets of the taxpayer as well as the willingness of the taxpayer to disclose relevant information.⁸⁷
- 1.96 The ATO also retains discretion to vary or revoke a DPO at any time.⁸⁸ A person aggrieved by the making of a DPO may apply to the Commissioner's discretion, or appeal to a Supreme Court or the Federal Court of Australia (Federal Court).⁸⁹ To maintain a DPO, the ATO must be able to demonstrate to the court that the DPO is required for revenue reasons and that the recoverability of tax owing will be affected by the departure of the taxpayer from Australia. A DPO must not be used to punish a taxpayer.⁹⁰ The onus, however, is on the taxpayer to show that the DPO was wrongly made and the Commissioner need not give reasons for the contention that the decision was made on reasonable grounds.⁹¹
- 1.97 In determining whether there are 'reasonable grounds' to issue a DPO, the ATO will take into account all relevant facts and circumstances such as:
- whether a tax liability can be recovered, including whether known assets are sufficient to pay tax liabilities, are readily realisable and their location;
 - whether audits or recovery proceedings are in progress as well as whether the taxpayer is subject to criminal investigation;
 - the taxpayer's behaviours, such as alienating assets to associated persons, concealing assets or moving funds overseas; and
 - indications of overseas travel and the reasons for that travel.⁹²
- 1.98 Following the making of a DPO, regular reviews are undertaken to ensure that keeping the DPO in force is still appropriate or requires variation.⁹³

⁸⁵ *Taxation Administration Act 1953* ss 14R, 14S(1), 14U, 14Z.

⁸⁶ ATO, 'Enforcement Measures', above n 56, para [134]-[135].

⁸⁷ ATO, 'Enforcement Measures', above n 56, para [157]-[158].

⁸⁸ *Taxation Administration Act 1953* s 14T.

⁸⁹ *Taxation Administration Act 1953* s 14V(1).

⁹⁰ *Skase v Cmr of Taxation* (1991) 32 FCR 206 at 211; 92 ATC 4001, 4005.

⁹¹ *Poletti v Cmr of Taxation* (1994) 94 ATC 4639; *Briggs v DCT (WA)* (1985) 85 ATC 4569.

⁹² ATO, 'Enforcement Measures', above n 56, paras [140]-[141].

⁹³ *Ibid*, paras [151]-[152], [154]; ATO, 'Departure Prohibition Orders Guidelines' (Internal ATO document, June 2014).

Securities for tax debts

1.99 The ATO may require security to be provided against assets of a taxpayer or third party in relation to existing debts or future tax liabilities to, amongst other things, secure the process of debt collection.⁹⁴ It should be noted that taxpayers may also voluntarily offer the Commissioner security.⁹⁵

1.100 The ATO may seek to obtain security in a range of situations, such as where:

- a taxpayer requests the ATO to defer the time for payment of a debt or is seeking to pay a debt by instalments;
- a debt is subject to dispute and an arrangement has been made with the ATO;
- the taxpayer wishes to leave Australia but is not in a position to pay the debt before leaving;
- the taxpayer is seeking a DAC from the ATO; or
- the taxpayer appears to be dissipating assets or there is any other indication that the revenue may be at risk.⁹⁶

1.101 In deciding whether to take or require security the ATO may have regard to, amongst others, the following considerations:

- the quantum of the debt (taking into account any objection or appeal process);
- the period of time the debt has been outstanding;
- the taxpayer's ability to pay, including their other liabilities and arrangements made by other creditors to secure their debts;
- the taxpayer's compliance history; and
- the nature of the security being offered (for example, location, liquidity, value and equity in the security).⁹⁷

1.102 Securities may take any number of forms, but the ATO prefers a registered mortgage from the taxpayer or a third party over freehold property where there is sufficient equity in the property or an unconditional bank guarantee from an Australian bank. The ATO will consider the taxpayer's circumstances when determining the security sought.⁹⁸

94 ATO, 'General Debt Collection Powers and Principles' above n 48, paras [76], [79].

95 Ibid, paras [77], [83].

96 Ibid, para [80].

97 Ibid, para [86].

98 Ibid, paras [81], [87]-[88], [108].

Offsetting credits and debits

- 1.103 The ATO has advised that offsetting tax credits and debits occurs through both automatic and manual processes in ATO systems.⁹⁹
- 1.104 Division 3 of Part IIB to the TAA 1953 mandates the ATO to offset an amount owed to a taxpayer to reduce, in whole or in part, a taxpayer's debt. In certain situations provided for under the law, the ATO may issue a refund rather than offsetting those amounts with tax debts on application by the taxpayer.¹⁰⁰ Some laws, however, may require the ATO to pay part or all of the refund to other government agencies, such as to the Child Support Registrar, in certain circumstances.¹⁰¹
- 1.105 Amounts may also be offset between a taxpayer's accounts which the ATO maintains to record various obligations, payments and credit entitlements under the tax laws (that is, income tax account and activity statement account).¹⁰² There are a number of different types of credit amounts which the ATO may use to offset tax debts. For example, the ATO may apply the whole or part of a family tax benefit credit (other than child care benefits) to any primary tax debts.¹⁰³
- 1.106 The ATO may also issue a refund rather than offsetting amounts where the amount owing is:
- due but not yet payable;
 - subject to a payment arrangement and the taxpayer is complying with that arrangement; or
 - an amount to which the Commissioner has agreed to defer recovery proceedings.¹⁰⁴
- 1.107 For convenience, in this report, the criteria listed above are referred to as 'Offset Criteria'.
- 1.108 In deciding whether to issue a refund, ATO staff are expected to balance the collection of tax and impact on the wider community, such as on those taxpayers who have paid on time, with the issues faced by the subject taxpayer if an offsetting occurs, such as serious financial hardship. The decision is subject to normal risk assessment processes, including review of the taxpayer's compliance history. Accordingly, the ATO will not issue a refund where it is determined that:
- there is an unreasonable risk to revenue, for example, where a taxpayer is dissipating assets;

⁹⁹ ATO, Communication to the IGT, 18 November 2014.

¹⁰⁰ An exception to the general rule to offset is for certain small amounts where the costs associated with offsetting are excessive such that it is uneconomical to do so: ATO, *Offsetting of Refunds and Credits Against Taxation and Other Debts*, PS LA 2011/21, 3 July 2014, para [13]-[14].

¹⁰¹ ATO, *Offsetting Of Refunds and Credits Against Taxation and Other Debts*, PS LA 2011/21, 3 July 2014, paras [1]-[5], [9]-[10].

¹⁰² Ibid, para [1]-[5].

¹⁰³ Ibid, para [87].

¹⁰⁴ Ibid, para [18].

- the taxpayer is a promoter of schemes; or
- the taxpayer has a poor compliance history.¹⁰⁵

1.109 Where ATO staff do not adhere to the above factors, taxpayers are entitled to request a tax refund.¹⁰⁶

1.110 The tax authorisations in relation to decisions not to offset refunds are set out in the table below.

Table 1.12: ATO staff authorisations not to offset amounts

Officer level	APS1	APS2	APS3	APS4	APS5	APS6 and above
	\$5k	\$10k	\$25k	\$50k	\$250k	∞

Source: ATO, 'Taxation Authorisations Guidelines' (Internal ATO document, November 2014).

Insolvency actions

1.111 Insolvency refers to a person's or company's inability to pay all their debts as and when they become due and payable.¹⁰⁷ A person who is insolvent may become a bankrupt.¹⁰⁸ A company that is insolvent may be wound up in insolvency.¹⁰⁹

1.112 In deciding whether to take insolvency action, the ATO will have regard to:

- all of the taxpayer's relevant circumstances, such as whether the taxpayer can demonstrate its solvency (sufficient liquid assets to enable all debts to be paid within a reasonable period of time), making arrangements to pay their debts, or trading whilst insolvent;¹¹⁰
- the asset position of the taxpayer, such as whether there are assets which may be realised to satisfy the debt and whether assets have been improperly alienated as well as where there is a risk that payments made to the ATO will become voidable preference payments¹¹¹ or it is not possible to assess the financial position of the taxpayer;
- the size and nature of the debt, such as where a debt is disputed, and where it is necessary to prevent a debt from escalating;
- whether the future income of the taxpayer would allow the debt to be fully satisfied;
- the risk to revenue, such as if the taxpayer is dissipating their assets or deliberately limiting their ability to pay; and

¹⁰⁵ Ibid, para [16]-[18].

¹⁰⁶ Ibid, para [12].

¹⁰⁷ *Corporations Act 2001* s 95A; *Bankruptcy Act 1966* s 5(2)-(3).

¹⁰⁸ *Bankruptcy Act 1966* s 5(1).

¹⁰⁹ *Corporations Act 2001* s 459A.

¹¹⁰ ATO, 'Insolvency - Collection' above n 60, paras [10], [16]-[17].

¹¹¹ For example, a transaction is voidable where it results in a creditor receiving more than they would receive from a company if the transaction were set aside and the creditor were to prove for the debt in the winding up of the company: *Corporations Act 2001* ss 588FA, 588F.

- the cost of insolvency compared to the likely return and the need to prevent debts from escalating.¹¹²
- 1.113 Under the bankruptcy laws the taxpayer may be required to make contributions from their future income towards their bankrupt estate if their income exceeds a threshold level.¹¹³
- 1.114 The ATO may also enter into agreements or arrangements under the *Bankruptcy Act 1966* (Bankruptcy Act) or *Corporations Act 2001* (Corporations Act) as alternatives to pursuing bankruptcy or wind up actions. Under these arrangements, taxpayers present their creditors with proposals under which they would be required to discharge their debts, usually over time and by paying less than the full amount of the debt in full and final settlement.¹¹⁴ Two of these key agreements are provided for under Part IX and Part X of the Bankruptcy Act for individuals and deeds of company arrangement under Part 5.3A of the Corporations Act for companies.
- 1.115 The ATO will consider the above proposals on their merits. It will vote in favour of proposed arrangements or agreements which have no adverse features and can provide the Commonwealth with a greater proportion of the provable debt within a reasonable period than would be received under bankruptcy or liquidation. However, as a general rule, the ATO will not vote in favour of an arrangement under which non-cash items, such as shares or other property, are offered to creditors. This is due to the costs and difficulties that may arise in administering the transfer and sale of that property.¹¹⁵
- 1.116 In deciding whether to vote in favour of alternative agreement or arrangement, the ATO expects its staff to consider, amongst other things:
- any legal advice that was obtained by the ATO;
 - the contents, comprehensiveness and adequacy of relevant reports as to the statement of affairs, the proposal and the report prepared by the trustee or administrator;
 - any liabilities not yet established, such as unissued assessments;
 - whether the debtor has made appropriate arrangements to meet future tax liabilities and the likelihood that the proposals put forward would be achieved;
 - the taxpayer's compliance history, including the extent and seriousness of any taxation offences which may have been committed;
 - any association between the debtor and other creditors;
 - other matters that are considered to be of public interest; and
 - the tangible benefit to the Commonwealth revenue that is expected to be gained from any proposed arrangement.¹¹⁶

112 ATO, 'Insolvency - Collection' above n 60, para [11].

113 Ibid, para [13].

114 Ibid, para [18].

115 Ibid, para [29]-[31].

116 Ibid, para [32].

- 1.117 The ATO has issued staff with a number of different authorisations relevant to decisions to commence insolvency actions. The key authorisations are outlined in the table below.

Table 1.13: ATO staff authorisations in relation to insolvency actions

	Officer level								
Type of action	APS1	APS2	APS3	APS4	APS5	APS6	EL1	EL2	SES
Creditor's petition in bankruptcy or application for winding up									
Institute	No	No	No	\$350K	\$1m	\$5m	∞	∞	∞
Withdraw	No	No	No	\$100K	\$1m	\$5m	∞	∞	∞
Accept dividend < 100c per \$									
	No	No	\$250k	\$1m	\$2m	\$5m	∞	∞	∞
Defer legal action									
Period	No	No	12 mths	18 mths	24 mths	∞	∞	∞	∞
Amount	No	No	\$150k	\$500k	\$1m	\$2.5m	∞	∞	∞

Source: ATO, 'Taxation Authorisations Guidelines' (Internal ATO document, November 2014).

- 1.118 The extent of ATO initiated insolvencies relative to those initiated by other creditors are shown in the table below.

Table 1.14: ATO-initiated insolvency action

		2011–12	%	2012–13	%	2013–14	%
Bankruptcies	ATO-initiated	519	2%	320	2%	565	3%
	Total	22,176		20,874		18,592	
Wind-ups	ATO-initiated	1,555	14%	1,071	10%	1,333	15%
	Total	10,818		11,192		9,916	

Source: Commissioner of Taxation, *Annual Report 2013–14* (2014).

- 1.119 The table above shows that the majority of insolvencies are not initiated by the ATO. Where the ATO does initiate insolvency, it initiates more company wind ups than bankrupting individuals.
- 1.120 More detailed statistics in the table below show the value of debt subject to ATO-initiated insolvency and the amounts recovered.

Table 1.15: Debt recovered as a result of ATO-initiated insolvencies

	2012–13			2013–14		
Taxpayer segment	Balance	Received	%	Balance	Received	%
INB	\$26,551,615.17	\$96,207.44	0.4%	\$29,997,901.10	\$184,635.76	0.6%
MIC	\$899,637,270.80	\$7,074,548.12	0.8%	\$458,035,407.30	\$14,848,027.93	3.2%
NFP	\$910,645.65	\$22,243.32	2.4%	\$887,031.12	\$40,311.71	4.5%
SME	\$71,309,849.22	\$4,261,532.86	6.0%	\$173,412,921.46	\$15,464,041.97	8.9%
Total	\$998,409,380.84	\$11,454,531.74	1.1%	\$662,333,260.98	\$30,537,017.37	4.6%

Source: ATO Communication to the IGT, 9 October 2014.

- 1.121 The table above shows that the ATO generally receives very little as a result of insolvency actions and shows that most insolvency action relates to small businesses and individuals.

Disputed debt

- 1.122 Unlike commercial debts, the law permits tax debts arising from disputed assessments to be recovered by the ATO before those disputes are resolved and appeal rights are exhausted. The fact that there is a dispute concerning the underlying tax liability does not defer the requirement to pay the tax and the Commissioner is entitled to take recovery action.¹¹⁷ However, if the dispute is resolved in the taxpayer's favour (in whole or in part), interest may be payable on the tax reversed.
- 1.123 As a general principle, the ATO expects that all debts, including those subject to dispute, will be paid on time.¹¹⁸ The ATO's approach to recovering disputed debts follows the risk of non-payment perceived by the ATO on the basis of all the relevant facts which may be continually assessed throughout the dispute.¹¹⁹
- 1.124 Where the ATO considers the dispute to be 'genuine' and there is a lower payment risk, the ATO may offer the taxpayer a '50/50 arrangement'. Under these arrangements taxpayers are required to pay all undisputed amounts and 50 per cent of the disputed debt excluding penalties – the ATO having agreed to such an exclusion in a previous IGT review.¹²⁰ In return, the ATO will defer recovery of the remaining balance of the disputed debt until 14 days after the objection, review or appeal is determined and will remit 50 per cent of the GIC that would otherwise accrue on the balance of the disputed debt.¹²¹
- 1.125 Where a taxpayer chooses not to enter into a 50/50 arrangement and there is an unacceptable level of risk associated with the case, the ATO will commence recovery action. However, the non-pursuit of recovery action by the ATO does not constitute formal deferral. Indeed, at the review or appeal stage the ATO has amended its policy during the IGT's review, such that recovery action will commence for unpaid disputed debts where formal deferral has not been granted.¹²²

117 *Taxation Administration Act 1953* ss 14ZZM, 14ZZR; *Deputy Commissioner of Taxation v Tropitone Furniture Co Pty Ltd* (1991) 22 ATR 361.

118 ATO, *Recovering Disputed Debts*, PS LA 2011/4, 26 February 2015, paras [9].

119 *Ibid*, paras [5]-[6].

120 IGT, *Review into the Australian Taxation Office's administration of penalties* (2014) para 2.49, Recommendation 2.2.

121 ATO, 'Disputed Debts' above n 118, paras [27]-[28], [36].

122 *Ibid*, paras [39]-[41].

- 1.126 In higher risk cases, the ATO will refuse or rescind a 50/50 arrangement and may commence collection action before a dispute is finalised, such as seeking judgment and execution thereof. In certain cases subsequently reassessed as being lower risk, the ATO may defer legal action if taxpayers can meet the requirements for deferral or provide an undertaking to the court that payment will be made within 14 days of the court's decision if the ATO is successful.¹²³
- 1.127 Where the level of risk necessitates legal action, the ATO may instead require:
- acceptable security to be provided or the payment of the debt in full or by instalments; or
 - 50 per cent of the disputed debt with the balance paid by instalments or acceptable security to be provided.¹²⁴
- 1.128 The above approach to disputed debts is illustrated in a process map in Appendix 5.
- 1.129 Notwithstanding the debt recovery powers of the Commissioner, the Federal Court and State Supreme Courts retain jurisdiction to stay proceedings for recovery where the taxpayer demonstrates special circumstances which justify a departure from the aim of prompt payment of tax.¹²⁵ In doing so, the court will have regard to avoiding an abuse of court process, such as through vexatious claims and ascertaining the requirements of justice in the particular circumstances. The court may also impose conditions in granting a stay of application which protects government revenue.¹²⁶

ATO ORGANISATIONAL STRUCTURE FOR DEBT MANAGEMENT

- 1.130 The Debt Business Line (DBL) is responsible for the overall management of tax debts payable to the ATO and is headed by a Deputy Commissioner. The DBL along with two other business lines belong to the Service Delivery Sub-plan (SDSP). The SDSP is within the People, Systems and Services Group. The reporting lines of the heads of these areas are set out in Figure 1.6 below.

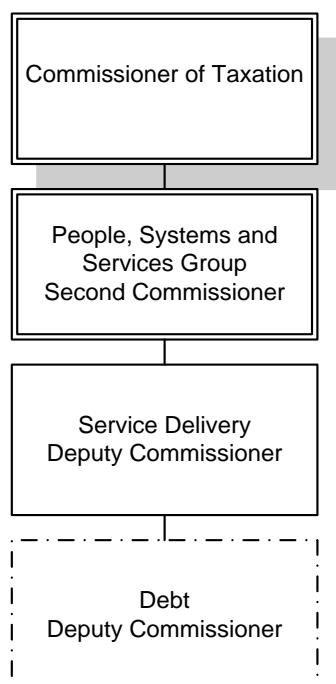
¹²³ Ibid, paras [44], [46]-[47], [49].

¹²⁴ Ibid, paras [52].

¹²⁵ *Re Roma Industries Pty Ltd* (1976) 76 ATC 4113; *Snow v DCT* (1987) 87 ATC 4078, 4090; *Held v DCT (Vic)* (1988) 88 ATC 4315.

¹²⁶ *Dalco v FCT* (1988) 88 ATC 4649; *Re Verma; Ex Parte DCT (NSW)* (1984) 84 ATC 4864, 4868.

Figure 1.6: ATO debt organisational structure



Source: IGT analysis of ATO information.

1.131 The DBL focuses on addressing two key enterprise risks in its management of tax debts, which are:

- payment risk – the failure to ensure willing tax and superannuation payment participation leading to a decrease in revenue collection; and
- debt risk – the failure to effectively manage taxpayer engagement leading to growing and aging debt.

1.132 A detailed explanation of the ATO's approach to risk management is contained in Chapter 2 of the IGT's *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools*.¹²⁷

1.133 In addition to the management of tax debts, the DBL also has a responsibility for improving the efficiency of ATO systems and processes to make it easier for taxpayers to meet their tax obligations as well as the prosecution and legal recovery aspects of ATO debt recovery activities.¹²⁸

Business units of the DBL

1.134 Until recently, the DBL had three units which conducted various debt recovery activities called 'Early Collections', 'Firm Action' and 'Strategic Recovery'. The responsibilities of each unit with respect to the activities they undertook are set out in the table below.

¹²⁷ IGT, *Review into Aspects of the Australian Taxation Office's use of Compliance Risk Assessment Tools* (2013) ch 2.

¹²⁸ ATO, Communication to the IGT, 7 October 2014.

Table 1.16: Responsibilities of the former units of the DBL

Activity / Product	Early Collections	Firmer Action	Strategic Recovery
Release	Yes	No	No
Payment arrangement	Yes	Yes	Yes
Remission of GIC	Yes	Yes	Yes
Non pursuit	Yes	Yes	Yes
Garnishee	Yes	Yes	Yes
DPN	No	Yes	Yes
S459e	No	Yes	Yes
Summons	No	Yes	Yes
Bankruptcy	No	Yes	Yes
Creditor's Petition	No	Yes	Yes
Wind-up	No	Yes	Yes
Judgment	No	No	Yes
DPO	No	No	Yes
Securities	No	No	Yes
Disputed Debt	No	No	Yes

Source: ATO Communication to the IGT, 12 December 2014.

Note: 'release' refers to release from payment of certain tax liabilities where a taxpayer will suffer serious financial hardship; 'non-pursuit' refers to decisions by the ATO not to pursue recovery action where debts are irrecoverable at law or uneconomic to pursue; 's 459E' refers to statutory demands served by the Commissioner as a creditor under the corporations law; 'summons' refers to processes taken by the ATO to have the court recognise that the debt is duly owed; 'judgment' refers to processes by which the ATO seeks to execute on the judgment.

- 1.135 However, as of November 2014, the ATO has merged the three previous units to form two units, 'Early Intervention' (EI) and 'Significant Debt Management' (SDM). The EI unit now focuses on 'single piece, high volume low-medium touch responses' whereas the SDM unit focuses on 'high value or high consequence taxpayers who represent an increased risk to revenue and integrity' of the tax system. The types of debt recovery activities which each unit undertakes are outlined in the table below. The ATO notes that this may change as it is still in the process of transitioning to the new approach.¹²⁹

Table 1.17: responsibilities of the new units of the DBL

Activity / Product	Early Intervention	Significant Debt Management
Release	Yes	No
Payment arrangement	Yes	Yes
Remission of GIC	Yes	Yes
Non pursuit	Yes	Yes
Garnishee	Yes	Yes
DPN	Yes	Yes
S459e	No	Yes
Summons	No	Yes
Bankruptcy	No	Yes
Creditor's Petition	No	Yes
Wind-up	No	Yes
Judgment	No	Yes

¹²⁹ ATO, Communication to the IGT, 12 December 2014.

Table 1.17: responsibilities of the new units of the DBL (continued)

Activity / Product	Early Intervention	Significant Debt Management
DPO	No	Yes
Securities	No	Yes
Disputed Debt	No	Yes

Source: ATO Communication to the IGT 12 December 2014.

Note: 'release' refers to release from payment of certain tax liabilities where a taxpayer will suffer serious financial hardship; 'non-pursuit' refers to decisions by the ATO to not pursue recovery action where debts are irrecoverable at law or uneconomic to pursue; 's 459E' refers to statutory demands served by the Commissioner as a creditor under the corporations law; 'summons' refers to processes taken by the ATO to have the court recognise that the debt is duly owed; 'judgment' refers to processes by which the ATO seeks to execute on the judgment.

Interface with compliance units and activities

1.136 The ATO developed principles by which the DBL and compliance business lines should engage with each other. The principles are intended to help optimise collection opportunities and improve the overall management of audit raised liabilities. The ATO expects that improved collaboration between the compliance business lines and the DBL would enable compliance staff to be more conscious of a taxpayer's obligation to pay liabilities raised. As a result, the ATO expects that cases would be escalated and progressed more efficiently to the DBL.¹³⁰

1.137 The four key principles that the ATO has developed in this regard are:

- a commitment to working together, while recognising the need for balance, and understanding the resourcing limitations;
- closing the gap between the end of a compliance activity (for example, audit or complex risk assessment) and payment conversations aimed at collecting liabilities;
- continuing conversations and direct engagement, where appropriate; and
- commitment to working together to resolve emerging issues.¹³¹

1.138 The ATO has advised that these principles are supported by processes which allow the escalation of debt collection recommendations to the DBL where there is an indication that taxpayers are unable or unwilling to pay.¹³²

130 ATO, 'Overarching Principles: Active Compliance and Debt' (Internal ATO document, 22 January 2014) p 4.

131 Ibid, p 7.

132 ATO, 'Active Compliance Debt project: Tier 3 Project Closure Report' (Internal ATO document, 21 June 2012).

EVOLUTION OF ATO DEBT MANAGEMENT STRATEGIES

- 1.139 The ATO's debt management strategies have evolved since the establishment of the DBL in the early 2000s to manage debt collection and seek to apply appropriate approaches across debt types. Prior to the establishment of this business line, debt was managed in various business lines dealing with particular types of taxpayers or types of taxes. It was believed that each type of tax debt required specialist treatment.
- 1.140 The ATO has advised that the DBL's debt management strategies focus on encouraging compliance. Initial strategies were based on an approach called the 'V curve', referring to the pattern of debt collections over time in response to collection and recovery actions. The type of focus a debt case received generally depended on the amount of debt outstanding.

External debt collection agencies

- 1.141 The Organisation for Economic Co-operation and Development (OECD) has cautioned that,

Delegating functions to the private sector has several legal and policy implications that need to be considered. Tax debt is regulated by tax laws which can complicate things for private collectors. Given the level of public scrutiny and risk of violation of privacy, comprehensive governance and quality assurance frameworks associated with the referral of debts to private collection agencies are essential.¹³³

- 1.142 A number of overseas revenue authorities use EDCAs to assist with the collection of tax debts with some concluding that such use was uneconomical.¹³⁴ For example, in the United States, the Internal Revenue Service (IRS) used private collection agencies (or EDCAs) over the 1996–1997 and 2006–2009 periods and terminated both programs as they lost money when opportunity costs were taken into account.¹³⁵ In both programs the IRS did not authorise the EDCAs to collect tax debts as they were used to assist in the IRS' collection activities, for example, locating taxpayers and securing commitments to pay their debts.
- 1.143 Furthermore, a recent proposal to use EDCAs in the United States has been the subject of public criticism for a number of reasons, including:
- that EDCAs have a profit maximising objective which is fundamentally different to government's objective of maximising long-term compliance without causing financial hardship for taxpayers;
 - the IRS had referred to EDCAs lower income taxpayers who may have been pressured into unaffordable commitments which, when defaulted, were considered additional non-compliance by the IRS and adversely impacted their ability to access payment assistance in future;

¹³³ OECD, 'Tax Debt Management', above n 45, p 78.

¹³⁴ Ibid, p 79.

¹³⁵ Letter from National Taxpayer Advocate to Congress (United States), 13 May 2014, pp 4–5.

- EDCAs potentially misusing IRS-provided information, such as for the collection of commercial debts; and
 - EDCAs not being exposed to the same penalties that apply to the IRS where taxpayer protections are violated.¹³⁶
- 1.144 Up to 2005, the ATO did not use EDCAs and its debt collection activities had traditionally focussed on functional areas addressing specific debt types through predominantly mail-based campaigns. However, overall debt holdings continued to grow largely influenced by the flow of debt each year accumulating to a backlog of approximately 1.5 million cases.¹³⁷
- 1.145 To address the backlog, the ATO had prioritised its broad collection action towards high volume, high collection strategies for debt cases, particularly focussing on new and escalating debts. Consequently, fewer resources were directed at a gradually increasing base of low value debtors.¹³⁸
- 1.146 To manage the accumulation of lower value debts, the ATO commissioned a pilot during 2005–06 to test the viability of utilising an established EDCA to assist with resolving certain cases within this group.
- 1.147 Following the pilot, the ATO established a panel of EDCAs¹³⁹ in September 2011 for an initial period of two years with two one-year performance based extension options. The EDCAs are currently engaged under the last option for renewal which will expire on 27 September 2015.
- 1.148 Under the terms of the contracts with EDCAs, continuation of services through the extension provisions is subject to satisfactory performance as measured through KPIs. In addition, each EDCA is required to provide an annual performance report to the ATO and undergo quarterly performance reviews.
- 1.149 The ATO has advised that, from 28 September 2011 to 30 June 2013, a total of 801,376 cases had been referred to panel EDCAs representing a total value of \$3.601 billion. Actual collections for this period were approximately \$2.363 billion.¹⁴⁰
- 1.150 The debt cases referred to EDCAs are contractually defined. The types of debts referred to the EDCAs include income tax, SGC and GST.

¹³⁶ Ibid, pp 6-10, 12-14.

¹³⁷ ATO, Communication to the IGT, 1 December 2014.

¹³⁸ Ibid.

¹³⁹ The current EDCA panel consists of Dun and Bradstreet, Recoveries Corporation Group Limited, Baycorp Collection Services Pty Ltd and Probe Group Pty Ltd.

¹⁴⁰ ATO, Communication to the IGT, 11 July 2014.

- 1.151 The ATO has also advised that eligibility for referral and retrieval is determined by a weekly process which is illustrated in Appendix 3. The stages of the weekly process are case selection, referral selection, generation of data extracts on new and retrieved cases, transmission of the data extracts to EDCAs and generation of reports. Once referred to an EDCA, cases continue to be assessed by this weekly process to ensure they remain eligible for referral. Cases are automatically retrieved when they no longer meet the criteria. The weekly processes are run at specific times that have been determined to factor in the needs of other cases and correspondence processes in the organisation.¹⁴¹
- 1.152 A referred case will generally remain with the EDCA for a period of up to 180 days. However, the ATO may retrieve or withdraw debt cases at any time, for any purpose.
- 1.153 The ATO's engagement with EDCAs and their collection of debts is explored further in Chapter 5.

Debt Reduction Team

- 1.154 The Debt Reduction Team was formed in 2011. The focus of the team is to reduce aged debt and to support the ATO's aim to maintain the proportion of collectable debt to collections at approximately 5 per cent.¹⁴² To achieve this proportion, the team identifies cases which are uneconomical to pursue or irrecoverable at law and 'writes off' the associated debt. The ATO reported internally that, in the 2012–13 financial year, the Debt Reduction Team had written off approximately \$603 million.¹⁴³

Debt Right Now program

- 1.155 The ATO believes that prior to the 2011–12 financial year, its approach to debt collection was 'random and ad hoc'.¹⁴⁴ As a result, the ATO has advised that in 2011 it implemented the Debt Right Now (DRN) strategy which aimed to improve the effectiveness of the ATO's debt collection process through the implementation of an improved risk-based collection model for case selection, amongst other things.¹⁴⁵ This collection model involves a risk assessment based on models of taxpayers' Capacity to Pay (C2P) and Propensity to Pay (P2P). The C2P model uses taxpayers' financial data from income tax returns and activity statements, amongst others things, to identify taxpayers at risk of insolvency.¹⁴⁶ The P2P model uses taxpayers' current income tax and activity statement data (for example, age and amount of debts) as well as prior behaviour, amongst other things, to identify taxpayers likely to repay their debts in full.¹⁴⁷

141 ATO, 'The Debt Referral Process: An Overview of the Processes and Procedures used for Selecting, Referring and Retrieving Debt Cases to External Collection Agencies (Internal ATO document, 2013) pp 4, 9.

142 ATO, 'Debt Reduction Team Review' (Internal ATO document, 2013).

143 Ibid.

144 ATO, 'Office Minute' (Internal ATO document, 10 September 2012).

145 ATO, 'Debt Right Now' (Internal ATO document, 22 November 2013).

146 ATO, 'Analytical Model C2P Income Tax: Service Design for Analytics Capacity to Pay Model (Internal ATO document, undated).

147 ATO, 'Analytical Model P2P Income Tax: Service Design for Analytics Propensity to Pay Model (Internal ATO document, undated); ATO, 'Office Minute' (Internal ATO document, 28 July 2014).

- 1.156 The treatment of debt cases consists of a series of actions that progressively escalate from 'softer' actions, such as reminder letters, through to 'firmer' actions, such as garnishee notices, DPNs and if the debts remain unpaid, wind up or creditor's petitions. A case's risk assessment would identify the entry point into that linear series of treatment.
- 1.157 Figures 1.7 and 1.8 below outline the debt recovery action to be taken for various levels of risk.

Figure 1.7: DRN treatment chart for individuals

Individual		Differentiated Taxpayer Treatments								
		T1 Letters	T2 Outbound Call	T3 Outbound Call	T4 Outbound Call	T5 Garnishee	T6 Claim / Summons	T7 Judgment	T8 Bankruptcy notice	T9 Creditor's petition
		PIF	PIF	PIF	PIF	PIF	PIF	PIF	PIF	PIF
Risk indicator	C1 RMS: 0.1, 0.2 Standard demand after 21 days	F. PA	F. PA	F. PA	20% & PA	20% & PA	20% & PA	20% & PA	20% & PA	50% & PA+CC
	C2 RMS: 0.4, 0.5 Standard demand after 7 days	20% & PA	20% & PA	20% & PA	30% & PA	30% & PA	50% & PA	100%	100%	100%
	C3 RMS: 0.7, 0.8			20% & PA+CC	20% & PA+CC	30% & PA+CC	30% & PA+CC	50% & PA+CC	100%	100%
	C4 RMS: 0.3, 0.6, 0.9				50% & PA+CC	50% & PA+CC	100%	100%	100%	100%
						Tracked	Tracked	Tracked	Tracked	Tracked
		Early Intervention are briefed daily on the campaigns they will work on. Conversation guides are on SMART.					Firmer Action use reference cards to guide conversations and actions for each of the treatments.			
Glossary		PIF: Payment In Full	F. PA: Flexible Payment Arrangement	(x) %: Upfront Payment	PA: Payment Arrangement	PTP: Propensity To Pay	CC: Capacity Conversation			

Source: ATO.

Figure 1.8: DRN treatment chart for companies

Company		Differentiated Taxpayer Treatments						
		T1 Letters	T2 Outbound Call	T3 Outbound Call	T4 Outbound Call	T5 Garnishee	T6 DPN/459e	T7 Wind up petition
		PIF	PIF	PIF	PIF	PIF	PIF	PIF
Risk indicator	C1 CAC: 0.1, 0.2 IT: PTP risk Low	Standard demand after 21 days	F. PA	F. PA	F. PA	20% & PA	20% & PA	20% & PA
	C2 CAC: 0.4, 0.5 IT: PTP risk Med.	Standard demand after 7 days	20% & PA	20% & PA	20% & PA	30% & PA	30% & PA	50% & PA
	C3 CAC: 0.7, 0.8 IT: PTP risk High			20% & PA+CC	20% & PA+CC	30% & PA+CC	30% & PA+CC	50% & PA+CC
	C4 CAC: 0.3, 0.6, 0.9				50% & PA+CC	50% & PA+CC	100%	100%
						Tracked	Tracked	Tracked
		Early Intervention are briefed each day about the campaigns they will work on. The conversation guide for each campaign is available on SMART.					Firmer Action use reference cards to guide conversations. Business Viability Assessment undertaken to substantiate viability of business.	
Glossary		PIF: Payment In Full	F. PA: Flexible Payment Arrangement	(x) %: Upfront Payment	PA: Payment Arrangement	PTP: Propensity To Pay	CC: Capacity Conversation	

Source: ATO.

- 1.158 The above figures demonstrate that where taxpayers did not engage with the ATO or where acceptable payment arrangements could not be negotiated, the severity of the ATO's action's increased progressively. Payment arrangements that were considered acceptable were also a function of the C2P and P2P models as well as tools, such as the BVAT. The early treatments (T1 to T4) were largely attempts to engage with taxpayers and entering into payment arrangements where necessary and which were conducted by the Early Collections unit. Firmer actions, such as garnishee notices and DPNs (T5-T6) were used by the Firmer Action unit. If necessary, the Strategic Recovery unit would issue section 459E statutory demands or take insolvency action. As previously mentioned, the ATO recently merged its DBL units.
- 1.159 Under the DRN strategy, higher risk cases were given priority.¹⁴⁸ Lower risk and value cases, on the other hand, were expected to be addressed primarily through 'self-finaliser models', which identify taxpayers likely to pay their debts without any ATO intervention, and low cost treatments for others, such as referral to EDCAs.¹⁴⁹ The debt case lifecycle under the DRN strategy is also illustrated in Appendix 4.
- 1.160 The ATO has advised that it has achieved a reduction in collectable debt, an increase in payments in full and more sustainable payment arrangements following the introduction of the DRN strategy.¹⁵⁰ Additionally, an ATO post-implementation review of the DRN strategy reported that it had improved end-to-end efficiency.¹⁵¹

The Business Viability Assessment Tool

- 1.161 Before the implementation of the BVAT, the ATO's approach to debt collection 'did not necessarily focus on the factors critical to an effective decision'.¹⁵²
- 1.162 In October 2009, the ATO engaged an external consultant to co-design a business viability checklist. The ATO has advised that the aim was to ensure that it supported a level playing field by not extending payment arrangements to unviable taxpayers and eroding the competitive position of viable taxpayers in the process. Such a means was to be achieved through a methodical, structured and evidence-based approach. To this end, the BVAT draws on taxpayers' financial information to evaluate the viability of their businesses via a number of solvency and other measures. The checklist was refined over time to an online tool for ATO staff and subsequently published on the ATO's website in 2012.¹⁵³

148 ATO, 'Office Minute July 2014', above n 147.

149 Ibid.

150 ATO, 'News Extra' (Internal ATO document, 47(5), 2011) p 22.

151 ATO, 'Office Minute July 2014', above n 147.

152 ATO, 'Office Minute September 2012', above n 144.

153 ATO, Communication to the IGT, 18 July 2014.

- 1.163 The ATO has advised that the BVAT essentially provides a credit risk assessment of a taxpayer. It uses three years of historical financial information to determine whether a business is generating a profit that is sufficient to provide a return to the business owner while also meeting its commitments to business creditors or has sufficient cash resources to sustain itself through a period when it is not returning a profit.¹⁵⁴ From this information it can identify short and medium term problems, such as changing prioritisation of creditors, time to pay, time to be paid and changes in equity.¹⁵⁵ The BVAT also indicates the maximum monthly repayment capacity of the taxpayer. These figures provide the start of negotiations between the ATO and taxpayer and may be augmented by other tools or data as mentioned earlier in this chapter. When the BVAT indicates a taxpayer may not be viable, the ATO will refuse payment arrangements and direct taxpayers to seek financial advice.¹⁵⁶
- 1.164 However, the ATO has determined that the use of the BVAT by the former Firmer Action unit revealed that the, 'vast majority of payment arrangement decisions previously made were not supported by at least a basic understanding of the taxpayer's financial performance and position'. A significant portion of these arrangement decisions also involved 'high-risk' taxpayers.¹⁵⁷ As a result, the ATO now requires the use of the BVAT in instances where debts exceed \$50,000 and the proposed payment arrangement does not align with the ATO's risk assessment of the case.¹⁵⁸ The BVAT must also be used where there are concerns with the taxpayer's viability and before firmer recovery action is taken.¹⁵⁹
- 1.165 The ATO has also advised that there is compulsory induction training for officers who use the BVAT and has recently provided voluntary refresher training, on 'keying and interpretation' as well as 'analysis and interpretation'. There is also a BVAT site leader to provide support to officers.¹⁶⁰
- 1.166 During the review, the ATO has also advised that it is planning to release a BVAT 'app' which allows taxpayers to compare their performance against others in their industry by inputting high level financial data.¹⁶¹

154 ATO, *Business Viability Assessment Tool* (23 September 2013) <www.ato.gov.au>; ATO, 'Office Minute September 2012', above n 144.

155 ATO, Communication to the IGT, 14 December 2014.

156 Ibid.

157 ATO, 'Office Minute September 2012', above n 144.

158 ATO, 'Business Viability Assessment Parameters' (Internal ATO document, March 2014); ATO, 'DRN Company Matrix', above n 53.

159 ATO, 'Office Minute September 2012', above n 144, p 7; ATO, 'BVAT Parameters' above n 158; ATO, 'DRN Company Matrix', above n 53.

160 ATO, 'Standard Training Schedule - Firmer Action' (Internal ATO document, July 2014); ATO, 'Debt Skill Set - Work Activities' (Internal ATO document, undated); ATO, Communication to the IGT, 14 December 2014; ATO, Communication to the IGT, 2 March 2015; ATO, Communication to the IGT, 1 April 2015.

161 ATO, Communication to the IGT, 27 February 2015.

Independent viability assessment project

- 1.167 The ATO has concluded a pilot in 2011 where optional IVAs were conducted by a third party assessor. The ATO has reported internally that the aim of the pilot was to ensure that non-viable businesses are not supported to the detriment of viable businesses and to maintain a level playing field for business. The IVA enables an ‘arm’s length’ test on the viability of businesses with large tax debts before proceeding with costly and resource intensive recovery action. This assessment seeks to provide the ATO with assurance that actions are defensible and appropriate in such cases.¹⁶²
- 1.168 A tiered selection based on intensity, ranging from those with no taxpayer contact to comprehensive reviews with full access to taxpayer information was recommended due to the different types/sizes of taxpayers, the varying scope of reviews necessary and the costs which range from \$5,000 to \$20,000. It is also proposed that taxpayers bear the costs of these reviews.¹⁶³
- 1.169 To be eligible for a IVA, a case must have the following attributes:
- the taxpayer is a business with debts greater than \$500,000;
 - the taxpayer is willing to engage and work collaboratively as well as being prepared to submit financial information to the third party assessor;
 - the taxpayer’s information can be made available; and
 - ATO recovery action will not be compromised.¹⁶⁴
- 1.170 Other attributes which may indicate suitability for IVA include cases in which:
- the taxpayer claims viability/solvency;
 - arrangements continue to fail and debt is escalating;
 - there is wider community impact from ATO action or increased reputation risk to the ATO.¹⁶⁵

Debt Serviceability Tool

- 1.171 The DST is used for sole traders with less than \$50,000 in debt for salary and wage earners. It is based on the ‘Henderson poverty line’¹⁶⁶ (updated quarterly) which is also used by financial institutions. The ATO has advised that it adds a 20 per cent margin to apply less pressure on taxpayers. The tool was developed in conjunction with financial counsellors and the Financial Services Council. The DST, unlike the BVAT, is not publically available.

¹⁶² ATO, ‘Independent Viability Assessment Pilot – Evaluation’ (Internal ATO document, 2011) p 4.

¹⁶³ Ibid, pp 7-9.

¹⁶⁴ ATO, ‘Independent Viability Assessment: Case Referral Checklist’ (Internal ATO document, 2011).

¹⁶⁵ Ibid.

¹⁶⁶ The ‘Henderson poverty line’ benchmarks the disposable income required to support the basic needs of a family of two adults and two dependent children: Commonwealth, *Commission of Inquiry into Poverty* (1973)

Risk differentiation framework and engagement model

- 1.172 The ATO now plans to replace the previous DRN strategy with a 'Risk Differentiation Framework' (RDF), which the ATO reports will inform debt case selection based on certain tolerances and triggers¹⁶⁷ and prioritise cases where debt continues to escalate.¹⁶⁸ A more comprehensive discussion of RDF models can be found in the IGT's *Review into Aspects of the ATO's use of Compliance Risk Assessment Tools*.¹⁶⁹
- 1.173 In a piece of correspondence provided to the IGT by the ATO toward the end of the review, it was advised that the implementation of a new 'Analytics for Client Engagement (ACE) program' had commenced.¹⁷⁰ The advice indicated that the program aims to prevent debts from arising and, where debts do arise, customising the 'next best action' to resolve the debt effectively. Furthermore, the program is made up of a number of analytical models which are being developed and informed by ATO research as well as being supported by the RDF. A diagrammatic representation was also provided that gives an overview of this program - see Appendix 7.¹⁷¹
- 1.174 The ATO has advised that the above new approach is a reaction to the realisation that the post GFC climate requires a range of strategies to manage payment compliance. The ATO claimed that during the GFC, the mining industry kept payment compliance high as it was an industry with fewer taxpayers and a high level of compliance. However, as economic activity continues to move away from the mining sector to other industries, the ATO is responding by establishing a range of strategies for these industries to manage payment compliance.¹⁷²
- 1.175 Although the majority of taxpayers pay their tax liabilities on time as shown by the earlier statistics, the ATO has identified the need to address taxpayer's issues when they arise, making it easier for them to comply and to assist them to set themselves up for the future.¹⁷³
- 1.176 The ATO's engagement with taxpayers is expected to be in response to their risk as outlined in Figure 1.9 below.

¹⁶⁷ ATO, 'Debt Strategy 2014-18', above n 42.

¹⁶⁸ ATO, Communication to the IGT, 7 October 2014; ATO, 'Service Delivery Plan 2014-15' (Internal ATO document, 2014).

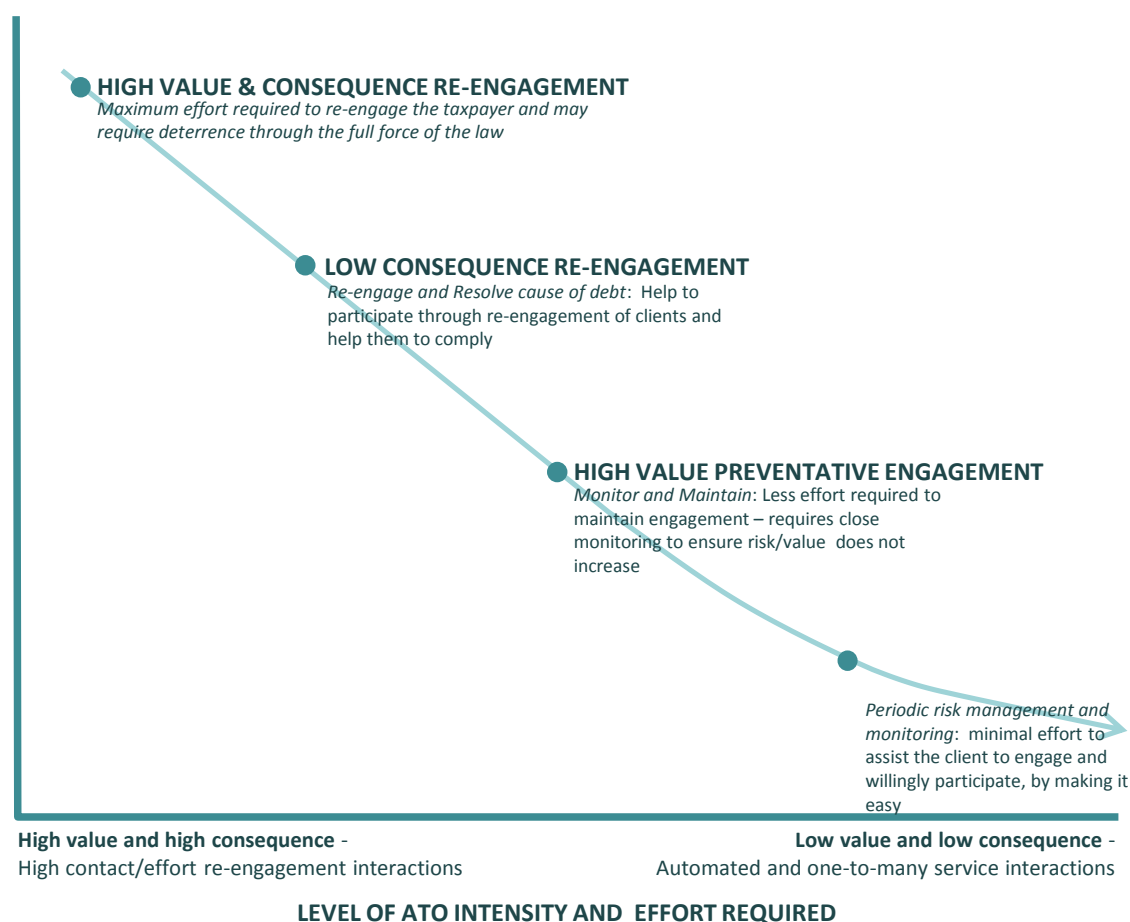
¹⁶⁹ IGT, Compliance Risk Assessment Tools review', above n 127.

¹⁷⁰ ATO, 'Compliance Pillars' diagram is shown in Appendix 7.

¹⁷¹ ATO, 'Achieving Payment Compliance Outcomes' (Internal ATO document, undated); ATO, Communication to the IGT, 11 March 2015.

¹⁷² ATO, Communication to the IGT, 1 December 2014.

¹⁷³ Ibid; ATO, 'Service Delivery Overview 2014-15' (Internal ATO document, undated); ATO, 'Service Delivery Plan', above n 168; ATO, 'Service Delivery Reinventing the ATO: Transforming our Business 2014-15' (Internal ATO document, undated); ATO, 'Debt Strategy 2014-18 Roadshow' (Internal ATO document, 2014).

Figure: 1.9: ATO debt engagement framework**ENGAGEMENT MODEL – BEHAVIOURAL RESPONSE MODEL**

Source: ATO, 'Debt Strategy 2014–18' (Internal ATO document, undated).

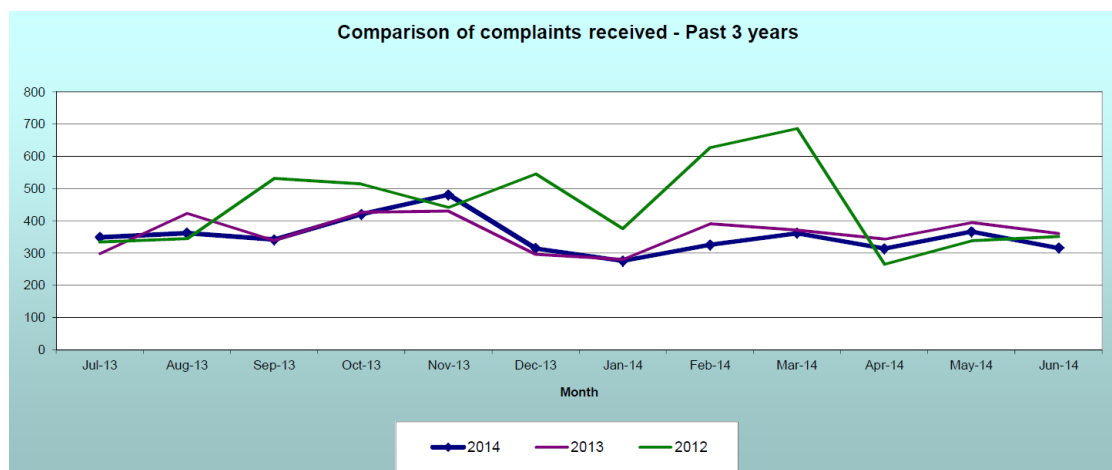
- 1.177 The above figure illustrates that ATO responses to taxpayers should be based on the risk they exhibit, such as whether they engage with the ATO or involve larger amounts of debt.
- 1.178 At the end of the review, the ATO also published a program blueprint for 'reinventing the ATO'. The blueprint describes the ATO's aspiration to build community confidence and willing participation in the tax system by 'ensuring that everyone pays the right tax at the right time ...'.¹⁷⁴

¹⁷⁴ ATO, *Reinventing the ATO: Program Blueprint – Summary* (2015) p 4.

DEBT COMPLAINTS

- 1.179 Despite the evolution of the ATO's debt management strategies, its approach to collecting debts has been a persistent cause of taxpayers' complaints accounting for 23 per cent of all ATO-related complaints received by the Commonwealth Ombudsman during the 2012-13 financial year.¹⁷⁵ The ATO has also received 3,720 complaints (containing 4,231 issues) with respect to its debt-related activities during 2013-14.¹⁷⁶ The ATO has asserted, however, that the quantum of complaints represents less than 0.5 per cent of the number of debt cases managed by the ATO during this period.¹⁷⁷
- 1.180 The table below sets out the trends in ATO debt-related complaints over the past three years.

Figure 1.10: Comparison of ATO complaints received over 2011-12 and 2013-14.



Source: ATO, 'Debt Ministerials and Complaints – Annual Report – Year Ending June 2014 (Internal ATO document, 2014).

- 1.181 Figure 1.10 shows that the level of complaints in 2012-13 and 2013-14 are similar but are relatively less compared to 2011-12.
- 1.182 The ATO has categorised the 3,720 complaints arising in the 2013-14 financial year according to the debt unit to which the complaint relates and whether the complaint was substantiated. The composition of the complaints is outlined in the table below.

¹⁷⁵ Commonwealth Ombudsman, Submission No 1 to House of Representatives Standing Committee on Tax and Revenue, *Inquiry into the Australian Taxation Office Annual Report 2012-13*, January 2014, p 5; Commonwealth Ombudsman, *Ombudsman 2012-2013 Annual Report* (2013) p 56.

¹⁷⁶ ATO, 'Debt Ministerials and Complaints - Annual Report - Year Ending June 2014 (Internal ATO document, 2014); ATO, 'Debt Compliments Data 2013-14' (Internal ATO document, undated).

¹⁷⁷ ATO, Communication to the IGT, 18 November 2014.

Table 1.18: Composition of debt complaints by debt area in 2013–14

	Auto Action	Early Collections	Firmer Action	Strategic Recovery, Super, Large	General	Total
Received	467	849	289	242	1,873	3,720
Finalised	512	999	335	261	1,665	3,772
Substantiated	56	247	57	63	270	693
% Substantiated (finalised)	10.94%	24.72%	17.01%	24.14%	16.22%	18.37%

Note: substantiated complaints are those where the ATO did not act in accordance with Taxpayers' Charter commitments.

Source: ATO, Debt Ministerials and Complaints – Annual Report– Year ending June 2014 (Internal ATO document, 2014).

1.183 Table 1.18 above shows that 3,772 complaints were finalised with 693 substantiated in the 2013–14 year (18.37 per cent of finalised complaints). Most complaints received were 'general' complaints (1,873), followed by complaints with respect to the Early Collections unit (849), 'Auto Action' treatments (467) and the Firmer Action unit (289). The areas of complaints with the greatest proportion of substantiated outcomes were in relation to the Early Collections unit (24.72 per cent), the 'Strategic Recovery, Super and Large' units (24.14 per cent) and the Firmer Action unit (17.01 per cent).

1.184 The top five specific complaints were:

- payment arrangement requests or review (for example, complainant had been refused a payment arrangement);
- responses not issued by the ATO (for example, ATO not responding to taxpayer correspondence);
- disagreed amounts of debt (for example, amounts outstanding as per the ATO records were not correct);
- offsetting credits with debits; and
- not understanding the debt (for example, why they have generated a debt).¹⁷⁸

1.185 Complaints received with respect to the ATO's firmer debt recovery activities are shown in Table 1.19 below.

¹⁷⁸ ATO, 'Debt Ministerials and Complaints', above n 176.

Table 1.19: Composition of debt complaints by debt recovery activities (2014)

	Yearly Issue Total	Yearly Upheld*	Upheld as % of yearly Issue Total			
	4252	991	23.31%			
	Total Quantity	% of Yearly Total	Total Upheld	% of Total Quantity of this issue type	% of Yearly upheld Total	% of Yearly Issue Total
459E Demand	14	50.00%	1	7.14%	100.00%	3.57%
Bankruptcy	28	100.00%	3	10.71%	300.00%	10.71%
Departure Prohibition Order	1	3.57%	1	100.00%	100.00%	3.57%
Director Penalty Notice	22	78.57%	3	13.64%	300.00%	10.71%
FTL - Remission Review	87	310.71%	9	10.34%	900.00%	32.14%
Garnishee	211	753.57%	22	10.43%	2200.00%	78.57%
GIC - Remission Review	183	653.57%	23	12.57%	2300.00%	82.14%
Hardship - Release/Relief	40	142.86%	8	20.00%	800.00%	28.57%
Insolvency	30	107.14%	10	33.33%	1000.00%	35.71%
Judgement	17	60.71%	1	5.88%	100.00%	3.57%
NILA	6	21.43%	1	16.67%	100.00%	3.57%
Offsetting Debt Internal	242	864.29%	28	11.57%	2800.00%	100.00%
Payment Arrangements	376	1342.86%	33	8.78%	3300.00%	117.86%
Re-raised Liability	49	175.00%	5	10.20%	500.00%	17.86%
Summons	24	85.71%	4	16.67%	400.00%	14.29%
Subtotal	1330		152			

* Upheld represents a finding in favour of the client

Note: The categories listed above represent those requested by the IGT for the purpose of this review. The remaining 2,992 types of complaints are spread across multiple categories such as Response not issued to correspondence the client has sent the ATO, Disagree with debt amount, Debt not understood, Penalty or interest imposition unreasonable, Dissatisfied with content of ATO correspondence, External debt collection process etc.

Source: ATO, 'Debt Complaints Count of Complaint Issue Templates – 2014 Financial Year' (Internal ATO document, undated).

- 1.186 Table 1.19 above shows that the debt recovery activities generating the three largest amounts of complaints were payment arrangements (376), garnishee notices (211) and offsetting debt (242). However, those activities with the highest proportion of upheld or substantiated complaints are DPOs (100 per cent), insolvency (33.33 per cent) and hardship release (20 per cent).

OTHER GOVERNMENT REGULATORS AND INTERESTED BODIES

- 1.187 In addition to the ATO, there are a number of other government agencies that have a role or an interest in the management of debts, especially those of small business. ASIC has regulatory responsibility with respect to business actions and is concerned with insolvent trading amongst other things.

- 1.188 ASIC has the power to investigate insolvency complaints and in doing so, may require people to produce books or answer questions at an examination.¹⁷⁹ ASIC also publishes monthly statistics on the number of companies entering external administration for the first time and the number of insolvency appointments.¹⁸⁰
- 1.189 The Australian Financial Security Authority (AFSA) fulfils official roles created by the *Bankruptcy Act 1966*, amongst others, to maintain high national standards of personal insolvency practice and procedure.¹⁸¹ AFSA cannot initiate insolvency proceedings but has the power to investigate complaints made by creditors or debtors against bankruptcy trustees and debt agreement administrators.¹⁸²
- 1.190 Other government agencies also have an interest in the viability of businesses, such as the ASBC, whose role is to assist small businesses and represent their concerns to government and its agencies, including the ATO in relation to recovering tax liabilities.

179 ASIC, *Our Role* (2014) <<http://asic.gov.au>>.

180 ASIC, *Insolvency* (2014) <<http://asic.gov.au>>.

181 AFSA, *Our Roles* (2014) <<https://www.afsa.gov.au>>.

182 AFSA, *About Regulation and Enforcement* (2014) <<https://www.afsa.gov.au>>.

CHAPTER 2 – ATO DEBT MANAGEMENT STRATEGIES

- 2.1 The OECD has highlighted the importance of revenue authorities management of tax debts,

Having appropriate strategies in place for debt management is particularly pressing in the present climate... where most revenue bodies face rising levels of tax debt with corresponding resource pressures and risks.¹⁸³

- 2.2 The total unpaid debt has continued to increase both in terms of quantum and as ratios of GDP and total net collections as mentioned in Chapter 1. Approximately three quarters of the unpaid debt is either collectable or subject to insolvency, with most of the amounts owed by individuals and micro businesses. Small business average times to pay creditors have also increased to levels which were observed during the GFC.¹⁸⁴
- 2.3 The ATO has recognised that its debt management strategies need to match the current and continuing challenges and has recently redesigned its strategies as described in Chapter 1.

SUMMARY OF STAKEHOLDER CONCERNS

- 2.4 Stakeholders have raised a number of concerns with the ATO's strategies for managing tax debts, including that:
- action needs to be taken to reduce the overall amount of tax debt by:
 - preventing debts from arising in the first place;
 - better targeting debt recovery and assistance activities;
 - commencing debt recovery and assistance activities earlier; and
 - conducting debt recovery and assistance activities more proportionately to taxpayers' circumstances and ensuring a level playing field between taxpayers;
 - the ATO should recover tax debts more fairly by better considering the impact of its debt recovery activities on others; and
 - more refined public reporting on the composition of tax debts to provide an insight into the causes or main areas which contribute to debts and the ATO's responses.

¹⁸³ OECD, Forum on Tax Administration, *Working Smarter in Structuring the Administration, in Compliance, and through Legislation* (2012) para [127].

¹⁸⁴ Refer to Chapter 1.

PREVENTION OF TAX DEBTS

- 2.5 Many stakeholders believe that better outcomes for both the ATO and taxpayers could be achieved if the ATO took proactive action which:
- better anticipated taxpayer debts and payment difficulties by drawing on available data to develop more sophisticated risk modelling;
 - prompted those taxpayers who may be experiencing financial difficulties to seek professional assistance to restructure, turnaround or enter into voluntary administration before debts arise; and
 - provided incentives to taxpayers to pre-pay anticipated tax liabilities.

ATO materials

- 2.6 The ATO's approach to debt under the DRN strategy took a risk-based approach to case selection¹⁸⁵ using models which predict a taxpayer's capacity to pay and propensity to pay as described in Chapter 1.¹⁸⁶ The taxpayer's risk determines the entry point into a linear treatment process (the riskier the taxpayer, the firmer the initial treatment) with escalating treatments if payment is not made or acceptable payment arrangements not entered.
- 2.7 However, productivity improvements alone have not addressed the increase in tax debt as reflected in the ATO's failure to reach its debt collection targets in the last two financial years.¹⁸⁷ The ATO has advised that it has commenced work to identify best practice and new strategies across the Australian Government and international revenue authorities. It is also utilising private sector expertise to inform the development of more effective debt management strategies aimed at preventing debts from arising.¹⁸⁸ Its current work in this area consists of:
- conducting research to understand the causes of small business tax debt accumulation as well as assessing the effectiveness of sanctions on the prevention of small business tax debt; and
 - developing more advanced analytical models to predict and prevent tax debts.¹⁸⁹
- 2.8 The ATO is also considering whether to incorporate its BVAT into commercially available accounting software to provide taxpayers and their advisers with the means to proactively monitor their viability.¹⁹⁰

185 ATO, 'Debt Right Now', above n 145.

186 ATO, 'Office Minute July 2014', above n 147.

187 Commissioner of Taxation 'Annual Report 2013-14', above n 35, pp 14, 17.

188 Ibid; ATO, Communication to the IGT, 11 September 2014; ATO, 'Debt Strategy 2014-18', above n 42, p 1; ATO, 'Service Delivery Plan', above n 168, pp 7, 15.

189 ATO, Communication to the IGT, 11 September 2014.

190 ATO, '5. Online BVAT Integrated Software (SD 230)' (Internal ATO document, undated).

Attitudinal and behavioural research

- 2.9 In January 2014, the ATO commissioned an external consultant to conduct a project called 'Attitudinal and Behavioural Research on the Prevention of Aged Debt' (BRP) which is based on similar work conducted by the New Zealand Internal Revenue Department (IRD) in 2011.¹⁹¹ The key outcomes of the BRP are to understand the drivers for the accumulation of tax debt by small businesses and subsequently develop better services and compliance strategies which, amongst other things, encourage willing payment of taxes and prevent debt accumulation.¹⁹²
- 2.10 Some of the key areas the project will consider include how small businesses make decisions concerning the payment of tax debt and relative payment priorities as well as how small business taxpayers form views about the behaviour of others.¹⁹³ Furthermore, key characteristics of taxpayers likely to fall into tax debts were investigated, including the type of taxpayer entity, number of employees, turnover, the age of the entity and the industry within which they operate.¹⁹⁴ The project will also consider the ATO's role in the prevention of tax debts and specifically whether its interventions 'promote, limit or prevent tax debt'.¹⁹⁵
- 2.11 Toward the end of this review, the ATO advised that they have commenced working with the IRD to compare the results of their respective research to provide 'new ideas on how to prevent the accumulation of aged debt by small businesses'. Additionally, the ATO expressed an intention to strengthen its corporate research capability more broadly to provide evidence which supports improved decision making.¹⁹⁶

Analytics project

- 2.12 Earlier, in May 2013, the ATO engaged an external consultant to develop analytical models that would improve its capability from simply descriptive analytics to more advanced predictive and prescriptive analytics (Analytics Project). This would be achieved by combining historical data, algorithmic models, variables, constraints and machine driven algorithms.¹⁹⁷ The project is expected to allow the ATO to, amongst other things, better prevent tax debts.¹⁹⁸

191 IRD, *Prevention of Aged Debts* (2011).

192 ATO, 'Project Outline: Attitudinal and Behavioural Research on the Prevention of Aged Debt' (Internal ATO document, April 2014).

193 Ibid.

194 ATO, 'Understanding Micro and SME Debt' (Internal ATO document, June 2014); ATO, 'Observation – Triggers of Debt' (Internal ATO document, March 2014).

195 ATO, 'Attitudinal and Behavioural Research', above n 192, p 7.

196 Ibid.

197 ATO, 'UTS project' (Internal ATO document, undated).

198 ATO, 'Attitudinal and Behavioural Research', above n 192.

- 2.13 The Analytics Project is designed around the delivery of a number of solutions. In relation to the prevention of tax debts, the relevant solutions to be delivered are:
- predict taxpayers that are likely to have tax debts, accumulate large amounts of debts and be costly for the ATO to manage; and
 - improve the accuracy of debt forecasting and identification of the influences which drive undesired taxpayer behaviours.¹⁹⁹
- 2.14 The development of the forecasting model was not originally conceived as part of the project. Accordingly, relevant work had not yet commenced at the time of the writing of this report.²⁰⁰
- 2.15 As mentioned in Chapter 1, the Analytics Project was recently incorporated into a new overarching project called the ACE program.²⁰¹ The BRP project is not incorporated within the ACE program, but rather seeks to inform it.

BVAT Integration Project

- 2.16 The ATO had commenced a project which sought to investigate the potential inclusion of the BVAT into commonly used accounting software to allow automated generation of viability assessments. This was expected to have a number of benefits, including allowing businesses to self-assess their viability in real-time without the need to depart from their current accounting systems.²⁰²
- 2.17 The BVAT integration project, however, was placed 'on-hold' by the ATO pending the outcome of a 'project stocktake'.²⁰³ The ATO has also advised that it has concerns whether embedding the BVAT into accounting software before Standard Business Reporting is implemented would render the BVAT ineffective in the new software environment.²⁰⁴ Furthermore, software developers have stated that, amongst other things, they need to more fully understand the level of investment required on their behalf and how this might be offset by potential benefits.²⁰⁵

¹⁹⁹ ATO, 'UTS project' above n 197.

²⁰⁰ Ibid

²⁰¹ ATO, Communication to the IGT, 11 March 2015.

²⁰² ATO, 'Debt Project Management Report' (Internal ATO document, August 2014); ATO, 'Online BVAT Software', above n 190.

²⁰³ ATO, 'Debt Project Management Report', above n 202.

²⁰⁴ ATO, Communication to the IGT, 14 December 2014.

²⁰⁵ ATO, 'Software Industry Consultation Summary' (Internal ATO document, March 2014).

Engagement strategies

- 2.18 One of the ATO's engagement strategies is the Debt Intermediary Program which seeks feedback from tax and insolvency practitioners, their representative bodies as well as other intermediaries to identify improvement opportunities and develop solutions to reduce debt by leveraging practitioners' influence over their clients. Key opportunities identified as part of this program included using:
- the insights from the BRP to modernise ATO communications including improving letters, the ATO website and other information sources (for example, publicising directors' responsibilities in the context of the director penalty regime);
 - the outcomes of the Analytics Project to identify potential debtors as part of the ATO's new Debt Engagement Framework; and
 - using email reminders for activity statement liabilities and payment arrangements.²⁰⁶
- 2.19 A feature of the Analytics Project is the 'self-finaliser' models. The aim of these models is to predict individual taxpayers who are likely to pay debts when due, without needing direct treatment action or 'self finalise' within a period of time.²⁰⁷ The ATO has advised that in one application of the self-finaliser models to the debt micro campaign (SMS reminders to taxpayers), 75 per cent of taxpayers predicted to pay on time, did pay on time. Additionally, 75 per cent of those predicted to not pay on time either paid late or never paid. As a result of the success of the model, the ATO considers that it became unnecessary to send approximately 20,000 SMS messages.²⁰⁸

Incentives to prepay anticipated debts

- 2.20 The ATO has consulted with the IRD and Her Majesty's Revenue and Customs (HMRC) on providing incentives to taxpayers to encourage prepayment of anticipated debts using existing tax payment systems to deduct tax at the source of income. One such system is the HMRC's 'coding out' program which allows taxpayers to prepay anticipated debts and is similar in concept to Australia's PAYG Withholding system for salary and wage earners. As a result of these consultations, the ATO is exploring 'front ending' collection to help prevent debts from arising. As part of this process, the ATO plans to consider whether small businesses, in the start-up phase, should be given a choice of entering the PAYG system to avoid having to pay their first year's tax bill and prepay their second year's tax bill in close succession.²⁰⁹ The ATO has publically commented that it is 'working on its systems to better integrate PAYG Instalments to the Income Tax Account'.²¹⁰

²⁰⁶ ATO, Communication to the IGT, 2 December 2014.

²⁰⁷ ATO, 'UTS project' above n 197.

²⁰⁸ ATO, 'Using Data in Smarter Ways to Improve Decisions, Services and Compliance: Income Tax (2014) SMS Payment Prompt' (Internal ATO document, November 2014).

²⁰⁹ ATO, Communication to the IGT, 1 December 2014.

²¹⁰ The Tax Institute, 'TAXvine' (12 December 2014).

- 2.21 Furthermore, one of the aims of the BRP is to better understand the effectiveness of incentives and sanctions on the prevention, management and reduction of small business tax debt through a behavioural economic tax experiment. It is uncertain, however, what specific sanctions and incentives the ATO will test but will include those which are non-financial in nature.²¹¹

IGT observations

- 2.22 The ATO data described in Chapter 1 has shown that the level of collectable debt has grown in quantity and as a proportion of GDP notwithstanding previous ATO strategies. Such growth in debt requires specific attention or government policy and public services would be adversely impacted. Stakeholders have suggested that, an essential aspect of the ATO's previous strategies was missing, namely a focus on anticipating debts and taking proactive action to prevent those debts from arising.
- 2.23 The ATO's previous debt management strategies sought taxpayer engagement once a debt had crystallised (that is, became due or payable). Such engagement aimed to stop debts from increasing or aging, however, it did not aim to prevent overdue debts. For example, the ATO's DRN risk and treatment matrices show that taxpayer engagement occurred only once a debt case was created.²¹²
- 2.24 The ATO, however, collects a large amount of information on taxpayer behaviours from their dealings with them, much of which is relevant to understand their payment performance. Analysing this data together with a range of current and historical information, such as taxpayers' previous payment behaviours and debt histories (including defaults)²¹³ as well as their financial circumstances, would enable the ATO to more accurately predict if a taxpayer may experience financial difficulties in the future which will adversely impact their ability to pay their tax debts. The ATO's ACE program aims to provide a framework for such an approach which is intended to be driven with the insights obtained from the ATO's supporting projects.
- 2.25 Importantly, the ATO's new strategy has components which focus on the prevention of tax debts as part of its broader plans to reduce the amount of tax debts.²¹⁴ Two key ATO projects – the BRP and the Analytics Project – may provide improved ATO understanding of small business taxpayers' attitudes and behaviours and lead to better predictions and strategies for debt prevention. The Analytics Project also aims to build on and validate the C2P and P2P models.

211 ATO, 'Attitudinal and Behavioural Research', above n 192, pp 5-7.

212 ATO, 'DRN Company Matrix', above n 53; ATO, 'DRN Individual Matrix', above n 53; ATO, 'Office Minute July 2014', above n 147.

213 A taxpayer's inattention to tax compliance and payment of liabilities is a common factor of poor business conduct and of pending business insolvency: ASIC, *Duty to Prevent Insolvent Trading: Guide for Directors*, Regulatory Guide RG217, July 2010, p 2, 21.

214 ATO, 'Service Delivery Plan', above n 168; ATO, 'Debt Strategy 2014-18', above n 42.

- 2.26 The above recent projects are encouraging and the IGT broadly supports their aims and intentions. However, a number of the aspects of these projects are either under development or not yet finalised and it is, therefore, difficult to assess their effectiveness until they are finalised and fully implemented. Accordingly, it has been challenging for the IGT to identify further improvement which aligns with the intent and aims of these recent projects. Nevertheless, the IGT believes that it is important to consider a number of key risks in relation to the projects.
- 2.27 First, there may be some overlap and interdependency between the BRP and Analytics Project based on an analysis of the project documents. Whilst the ACE program now incorporates the Analytics Project and will draw upon the insights of the BRP in developing analytical models, there may be a risk of incongruent or inefficient operational deployment. Such deployment has the potential to reduce the effectiveness of the initiatives where management oversight is not alive to these risks.
- 2.28 Secondly, there is a need for appropriate success measures that are aimed at validating the individual projects' findings which underlie the ACE program. As the OECD has said, 'Even the most sophisticated strategies for facilitating enforcing compliance are worth little if the tax owed is not actually collected'.²¹⁵ The ATO has recently advised that it has developed success measures (or 'acceptance criteria') for all projects within the ACE program. However, these specific measures were not available for consideration during this review. Accordingly, the IGT is not in a position to comment upon these or their effectiveness and believes that, in addition to success measures, post-implementation reviews would help assure the ATO that its strategies are effective and the underlying projects are having their intended effects.
- 2.29 Thirdly, whilst the ACE program is intended to apply to all taxpayer segments, the BRP, which informs the ACE program, only focuses on small businesses with individual and other taxpayers being excluded. However, as noted in Chapter 1, individuals are also significant contributors to tax debt representing between 15.34 per cent and 17.09 per cent of all collectable debt between the 2010-11 and 2013-14 financial years.
- 2.30 The IGT believes that the new ATO focus on taxpayer behaviours is more likely to achieve a sustained reduction in debt holdings over the longer term. However, in the interim, the IGT considers that the ATO should expand its projects from purely focusing on small businesses to include other major contributors to tax debts, such as micro businesses and individuals. Through these projects, the ATO could obtain useful information on the causes of cash flow and payment difficulties with respect to all these taxpayer types. Such information could then be used to develop targeted strategies, the implementation of which should result in substantial reductions in overall debt levels in the shorter term.

215 OECD, 'Structuring the Administration', above n 183, para [127].

- 2.31 Preventative interactions which assist taxpayers avoid falling into debt are particularly important for micro businesses as their financial management skills may vary widely given approximately 44 per cent of business insolvencies are said to be a result of poor strategic business decision making.²¹⁶
- 2.32 The IGT believes that more accurately identifying those taxpayers, who are likely to fall into debt, allows the ATO to proactively engage with them earlier and before a tax debt arises. However, in doing so, there is a balance that has to be struck. The ATO could be perceived as 'badgering' when no debt actually exists. For example, a taxpayer who may be intending to pay their debts on time would likely not appreciate a call from the ATO to simply remind them to pay their debt. Rather, they may prefer a call where the ATO describes its understanding of any potential financial distress and offers to discuss the need for a payment arrangement.
- 2.33 Some taxpayers also need reminders of upcoming debt payment obligations. The ATO is exploring the use of a range of methods, including sending targeted letters or SMS messages, providing an online facility for taxpayers to check and pay their debts and enabling functionality in the Tax Agent Portal which provides tax agents with a high level overview of all their clients' tax debts, due dates and payment reminders.
- 2.34 Difficulties with managing cash flows can adversely affect a micro businesses' ability to pay their debts on time. Accordingly, providing an easy means and incentives to prepay anticipated tax debts well before they become due and payable would assist taxpayers to better manage their cash flows whilst meeting their tax obligations.
- 2.35 As the OECD has observed, the more revenue authorities succeed in making taxpayers pay as they earn, the smaller the debt book will be.²¹⁷
- 2.36 In the IGT's view, the ATO would reduce the risk of late or non-payment if it made payment part of the normal system of doing business and as close to the event creating the liability as possible.
- 2.37 The ATO currently allows taxpayers to prepay anticipated debts if they contact the ATO first. This allows the ATO to stop automatically refunding credits.²¹⁸ In addition to allowing taxpayers to make ad hoc pre-payments, use of regular payment mechanisms, such as PAYG Instalments, may provide such a means without increasing compliance costs for taxpayers. The United Kingdom uses a similar means through its 'coding out' initiative which allows taxpayers to make voluntarily additional prepayments of taxes at the source of income. It also facilitates third party tax remitters to deduct an increased percentage of tax at the source of income.

²¹⁶ ASIC, 'Report 372', above n 2.

²¹⁷ OECD, 'Tax Debt Management', above n 45, p 18.

²¹⁸ ATO, Communication to the IGT, 12 February 2015.

- 2.38 By adopting a similar approach in Australia, taxpayers could remit extra amounts for future anticipated taxes to allow them to better manage their cash flows. Such an approach has positive behavioural aspects as some taxpayers find it easier to part with funds which are never actually received. The IGT believes there may be merit in the ATO investigating whether a similar mechanism could operate in Australia and whether legislative amendment would be necessary.
- 2.39 The ATO has also advised that it had recently released a tender for EDCAs which, amongst other things, seeks new strategies from the market to improve debt collection through better case management, allowing taxpayers to self-help and making it easier for them to pay.²¹⁹ The IGT considers that such consultation with debt professionals may provide the ATO with valuable insight on novel ways to prevent tax debts and fruitful options that would both assist taxpayers to meet their obligations as well as ensure that appropriate taxes are collected.
- 2.40 Improving micro business financial management skills is also an important means to prevent tax debts from arising as many insolvencies occur as a result of poor strategic management and inadequate cash flows as identified in Chapter 1. There are a number of key agencies which aim to assist small business, including ASIC and the ASBC.²²⁰ The IGT believes that there is scope for the ATO to work more closely with these other agencies to provide an integrated government approach to improving micro business financial management skills.
- 2.41 Although educative assistance has the potential to help businesses better manage their business and regulatory obligations, it will be ineffective for those businesses that are unaware or underestimate the risks of financial distress. For example, the level of tax liabilities for a micro business may not become apparent until they complete their tax reconciliations as part of the lodgment of their annual activity statements. Tax practitioners, however, are well placed to prompt their clients to seek business advice where they have access to almost real-time financial data and would be able to identify issues as they arise. In addition to prompting their clients to seek advice, tax practitioners may also be able to help businesses manage their cash flow by drawing on such assistance as ATO payment arrangements.
- 2.42 Submissions also suggested that the ATO could require taxpayers with a poor payment history to lodge activity statements more frequently, although indicators of financial distress may be identified more quickly by analysing the business' financial records in real time with the appropriate tools.

²¹⁹ ATO, Communication to the IGT, 18 November 2014.

²²⁰ The Government has indicated an intention to transform the ASBC into the Australian Small Business and Family Enterprise Ombudsman: The Treasury, 'Australian Small Business and Family Enterprise Ombudsman' (Discussion Paper, April 2014).

- 2.43 Embedding credit risk assessment tools into commonly used accounting software would help taxpayers to proactively self-assess their business' performance and viability without the ATO initiating any such contact or conducting such analysis. Relevantly the ATO has plans to incorporate the BVAT into commonly used accounting software. Such use of the BVAT could provide taxpayers, especially those with less business management experience, with 'alerts' of anticipated financial difficulties and the specific issues on which professional advice may be necessary to turn their businesses around. However, such plans are currently held in abeyance as software developers need to more fully understand the level of investment required on their behalf and how this might be offset by potential benefits.²²¹
- 2.44 The IGT considers that the BVAT's integration into commonly used accounting software would provide micro businesses a cost-effective means to manage their finances to pay creditors, including the ATO. Such integration also has the potential to help recover a substantial proportion (45 per cent) of all collectable tax debts owed by micro businesses. Accordingly, the ATO could encourage discussion on the benefits of incorporating the BVAT into accounting software, which could also include representations by insolvency practitioners and small business advocates.
- 2.45 The IGT also believes that the ATO's DST could be used by individual taxpayers to consider their cash flow and any necessary adjustments, particularly as they also appear to represent a significant proportion of those with unpaid tax debts. However, the DST is only available to internal ATO staff.²²² Therefore, the IGT believes that the DST should be made publically available to support individual taxpayers.
- 2.46 The ATO's BRP and ACE program may also help the ATO to identify taxpayers that may be experiencing financial distress before tax liabilities become due and payable. Such information could allow the ATO to identify those taxpayers that require prompting to take steps to assure themselves of their future capacity to pay, for example, by seeking the professional assistance of financial counsellors.²²³ These projects may also help the ATO identify suitable incentives to encourage taxpayers to seek such assistance which may, for example, include appropriate remission of GIC. Stakeholders have also supported such an option.

RECOMMENDATION 2.1

The IGT recommends that the ATO incorporate the following initiatives into its Analytics for Client Engagement Program or related projects aimed at minimising tax debt:

- (a) a program to identify the underlying causes of cash flow and payment difficulties for micro business and individual taxpayers and develop preventative strategies;*
- (b) an online facility which taxpayers and their advisers can use to prepay anticipated tax debts – for example through the myGov website and Tax Agent Portal;*

²²¹ ATO, 'Consultation Summary', above n 205.

²²² ATO, Communication to the IGT, 14 December 2014

²²³ Financial Counsellors can: suggest ways to improve your financial situation; explain your options and their consequences, including debt recovery procedures, bankruptcy and other alternatives; help you organise your finances and do a budget; refer you to other services, for example, a gambling helpline, family support, personal counselling or community legal aid: ASIC, *Financial Counselling* (3 March 2015) <<https://www.moneysmart.gov.au>>.

RECOMMENDATION 2.1 CONTINUED

- (c) *facilitate discussions with software developers, insolvency practitioners and small business advocates to promote the benefits of incorporating the business performance review tools (such as the ATO's Business Viability and Assessment Tool) into commonly used accounting software;*
- (d) *make publicly available a personal financial management tool such as the Debt Serviceability Tool; and*
- (e) *identification of taxpayers who are most likely to experience cash flow difficulties and encourage them to seek professional advice.*

ATO response: Agree

We are implementing a program of work which includes:

- an active research and analysis program aimed at building a deeper understanding of the causes of cash flow and payment difficulties, encompassing all taxpayer types and segments;
- preventative strategies including SMS reminders for taxpayers identified as likely to experience payment difficulties; and
- working with software developers to incorporate business performance review tools (referred to as a Business Performance Check) into commonly used accounting software.

The ATO is intent on making it easier for all taxpayers to manage their tax payments thereby avoid falling into debt. We are expanding our existing range of integrated digital solutions, products and services focused on client needs, making it easy to get things right and hard not to (Reinvention blueprint). Through co-design we will develop the most appropriate products based on the demands and expectations of the community.

TARGETING ATO DEBT ACTIVITIES

- 2.47 Many stakeholders believe that the ATO does not adequately target its debt recovery and assistance activities and resources to effectively minimise the quantum and age of tax debts. For example, stakeholders have commented that the ATO focuses on once-off taxpayers and those with smaller debts rather than on serial debtors and those who have larger debts.

ATO materials

- 2.48 As discussed in Chapter 1, in 2011, the ATO developed the DRN strategy which was to improve the targeting of debt collection through, amongst other things, the implementation of a risk-based collection model for case selection.²²⁴ This collection

²²⁴ ATO, 'Office Minute September 2012', above n 144; ATO, 'Debt Right Now', above n 145.

model involves a risk assessment based on models of taxpayers' capacity to pay and propensity to pay.²²⁵

- 2.49 The DRN strategy gave priority to higher risk and value cases.²²⁶ Lower risk and value cases were addressed through 'softer treatments', including through the 'self-finaliser models' which identify taxpayers who are likely to pay their debts without any ATO intervention or referral to EDCAs.²²⁷ Such approaches allow the ATO to direct resources to more complex cases.
- 2.50 The ATO is now transitioning from the DRN collection model to the RDF based strategy, which amongst other things, will inform debt case selection based on certain tolerances and triggers²²⁸ and prioritise cases where debt continues to escalate.²²⁹ The ATO has also advised that the treatments under the earlier mentioned ACE program will not necessarily follow a linear process as with the DRN strategy, but rather will be based on the 'next best action'. The ATO acknowledges that this may create perceptions of inconsistencies in the future.²³⁰
- 2.51 In addition to the above strategy, the ATO has also sought to identify and 'not pursue' those debts that are irrecoverable at law or uneconomical to recover.²³¹ The total value of these debts for the last three financial years is shown in the table below.

Table 2.1: Value of debt not pursued over 2010–11 and 2012–13

Year	Debt not pursued
2010–11	\$3.8 billion
2011–12	\$3.8 billion
2012–13	\$4.6 billion

Source: ATO Communication to the IGT, 1 April 2015.

- 2.52 The ATO has also sought an external consultant to evaluate the ATO's debt holdings to determine which debts are 'truly actionable' and identify segments of actionable debts that may be collected more effectively at a lower cost (Actionable Debt project). The consultant's proposal in relation to this project suggests that actionable debt can be identified by using taxpayers' assessment data. For example, assessment data could show a rapid deterioration in a taxpayer's financial circumstances indicating that the debt may not be actionable. It is envisaged that this work will reduce assessments not collected, identify non-collectable debt more accurately and increase the amount of debt collected.²³²
- 2.53 An overview of the consultant's proposal is reproduced in the figure below.

225 ATO, 'Office Minute July 2014', above n 147.

226 Ibid.

227 Ibid.

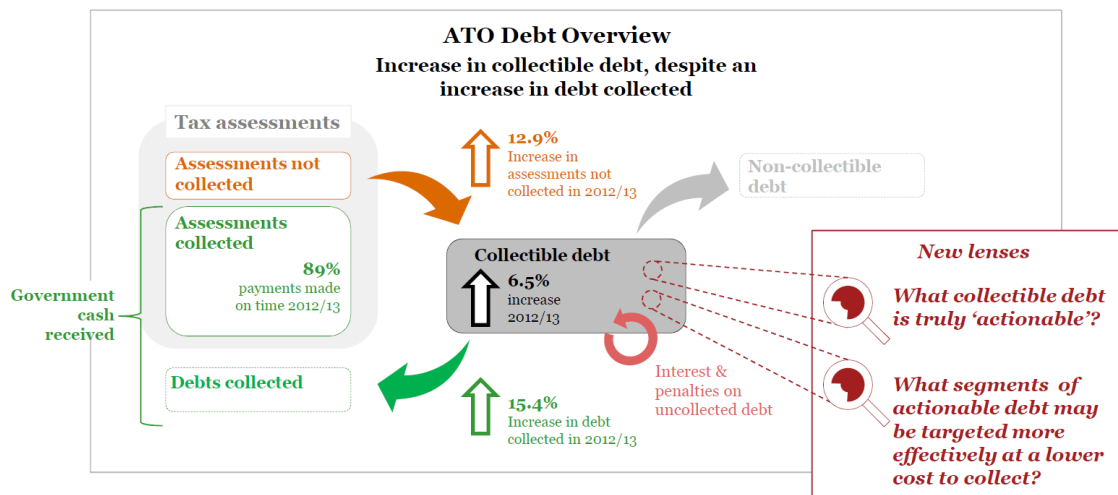
228 ATO, 'Debt Strategy 2014-18', above n 42.

229 ATO, Communication to the IGT, 7 October 2014; ATO, 'Service Delivery Plan', above n 168.

230 ATO, Communication to the IGT, 9 December 2014; ATO, Communication to the IGT, 12 December 2014.

231 ATO, 'Debt Reduction Team Review', above n 142.

232 ATO, 'Bringing a Fresh Lens to Assessing the ATO Debt Book' (Internal ATO document, undated); ATO, Communication to the IGT, 11 September 2014.

Figure 2.1: Consultant's proposal to identify actionable debt

Source: PWC, Australian Taxation Office – Bringing a fresh lens to assessing the ATO debt book Proposal (Undated).

IGT observations

- 2.54 In relation to targeting its debt activities, the ATO's acknowledgment that previous approaches to financial analysis and risk assessment were 'random and ad hoc'²³³ was an important first step. The evolution to the DRN strategy was also a positive next step albeit the ATO discovered that, if a linear approach was maintained, tax debt could not be reduced any further.²³⁴ As a result its strategies are evolving and transitioning into a more risk-based and tailored system that is, through the Debt RDF and 'next best action' approach.
- 2.55 The 'next best action' approach could use the ATO's own extensive data along with other available data sources to understand how taxpayers have reacted to different debt recovery actions in the past and to build models that predict which actions will be most effective in dealing with specific types of taxpayers.²³⁵ Such information could be used as a basis to more accurately determine the most appropriate intervention strategy to improve revenue flow. It will also allow the assessment of the effectiveness of such a novel approach.²³⁶
- 2.56 Therefore, the ATO's intended next step of moving to a more risk-based and tailored model seems promising. The insights from the ATO's Actionable Debt Project and ACE program should also allow the ATO to better focus its resources on 'higher priority' debts which are 'actionable' where taxpayers do not 'self-finalise'.
- 2.57 The nature of the debt environment is dynamic, however, as what works today may not work next year as taxpayer reaction also changes. Therefore, once the new approach is settled and the projects are incorporated into business as usual, it would be prudent for the ATO to conduct ongoing reviews to determine the effectiveness of its approach and identify areas for improvements.

²³³ ATO, 'Office Minute September 2012', above n 144.

²³⁴ ATO, Communication to the IGT, 12 December 2014.

²³⁵ OECD, 'Tax Debt Management', above n 45, p 22.

²³⁶ Ibid, p 15.

- 2.58 In addition to the new RDF and 'next best action' approach, the ATO is undertaking the BRP. One aspect of the BRP, which has been completed, identifies the common characteristics of small businesses with tax debts. The characteristics which the ATO has examined include entity type, age of business, industry sector and the most common type of debt outstanding (for example, those arising from the GST, PAYG, income tax, interest etc.). As noted previously, the BRP could be expanded to include other taxpayers which commonly have debts, such as individuals.
- 2.59 Towards the end of this review, the ATO has advised the IGT that it has begun to target particular taxpayer segments to address particular types of tax debts. The IGT is of the opinion that if such targeted campaigns drew on the above BRP findings, the campaigns could provide an effective method for the ATO to reduce outstanding tax debts more quickly as the new strategy and 'next best action' approach are progressively designed and implemented.
- 2.60 For example, the IGT analysis of ATO data in Chapter 1 has identified the two following areas that require particular attention:
- micro businesses with a turnover of less than \$500,000 whose debts (particularly non income tax debt) are no greater than six months old as they represent almost 30 per cent of total collectable debt in 2012–13 (approximately \$5.4 billion); and
 - individual taxpayers with debts greater than six months old (approximately \$1.6 billion in 2012–13) particularly as debts in this market segment appear to accumulate and become more difficult to recover over time.
- 2.61 In addition to targeting key areas giving rise to larger amounts of debts, the IGT considers that the ATO's targeting of debt strategies should also have the aim of engendering long term behavioural change. Rather than focus on debts as and when they arise, focusing on the debtor's behaviour could generate returns in later years where their payment behaviours have been improved as a result of the ATO's interactions.

RECOMMENDATION 2.2

The IGT recommends that the ATO, as it designs and implements new debt strategies,:

- (a) continue to use existing research findings to target debt activities to those taxpayer segments which comprise substantial amounts of recurrent and/or aged tax debts, such as micro businesses and individuals; and*
- (b) incorporate feedback loops to facilitate continuous improvement.*

ATO response: Agree

The ATO is progressively rolling out new strategies and targeted approaches based on advanced analytics and research. The ATO has shifted its approach to debt management in response to community feedback and the increasing level of debt in recent years. This shift is underpinned by our research findings and analytics and includes a greater focus on targeted approaches. We will continue to consult with and respond to community and staff feedback to ensure our approach and strategies are effective.

For example, our SMS preventative strategies include feedback loops from clients, representatives and staff, which has enabled us to review the effectiveness of the strategy, refine the population for each due date, and the wording of our messages.

DELAYED COMMENCEMENT AND PROPORTIONALITY OF ATO RECOVERY ACTIVITIES

- 2.62 Stakeholders have observed that, unlike the private sector, in many cases the ATO is slow to collect tax debts. They have asserted that, with respect to commercial debts, action is taken much sooner to recover the debt with those choosing not to pay their debts being treated appropriately. Furthermore, ATO inaction may exacerbate non-compliance and the need for firmer debt recovery action later. Such an outcome propagates the impacts of insolvent trading, including competitive impacts on taxpayers who do the right thing.
- 2.63 Stakeholders, however, are divided on whether the ATO's approach to debt recovery is proportionate. Some stakeholders believe that the current approach strikes a fair balance between the need to efficiently collect tax debts and financial accommodation to help taxpayers manage through adverse circumstances. Other stakeholders, however, have observed that the ATO takes disproportionate and undifferentiated action which does not adequately consider taxpayers' circumstances. They believe that a level playing field does not exist, asserting that taxpayers:
- with similar circumstances are not treated in the same way;
 - who are first-time debtors are treated more firmly than serial debtors; and
 - who are larger businesses, with larger debts, are able to negotiate and settle those debts more favourably than smaller business taxpayers, with smaller debts, who are aggressively pursued.
- 2.64 A number of stakeholders have also observed taxpayers becoming less engaged with the ATO due to a recent sudden shift from a softer debt collection approach during the peak of the GFC to a firmer approach in recent years which it is alleged occurred without warning. They also believe that any such shift in approach should be effectively and clearly communicated to ensure that taxpayers understand the ATO's reasoning and prevent perceptions of political motivation for such actions.
- 2.65 Greater transparency and education on ATO processes have been called for more generally as many taxpayers are unaware of, and do not understand, the ATO's debt-related procedures, including criteria for debt referral to EDCAs.

ATO materials

- 2.66 Broadly, the severity of the ATO's approach is intended to align with the overall perceived compliance risk of a taxpayer. This includes consideration of the taxpayer's capacity to pay and their past behaviours as well as the most effective debt recovery action.²³⁷ It should be noted that, during the GFC, the ATO had made adjustments to its debt practices to ensure the approach taken was appropriate given the downturn in economic conditions. For example, in response to the financial impact on businesses, the ATO granted activity statement lodgment deferrals as well as flexible and interest free payment arrangements.²³⁸
- 2.67 Following the GFC, the DRN strategy was developed to address the growth in collectable debt²³⁹ and resolve debt cases more quickly amongst other things.²⁴⁰ In a 2012 post-implementation review of the BVAT, the ATO found that the BVAT, in conjunction with the DRN strategy, led to faster progression of appropriate action for debt cases involving amounts greater than \$5,000.²⁴¹ However, a significant volume of cases remained unactioned for extended periods due to competing priorities.²⁴²
- 2.68 The new ATO debt management strategy recognises that a key debt risk is 'deterioration in payment behaviour'. Failure to engage taxpayers in a timely manner, that maintains positive payment behaviour, may lead to a decrease in revenue collection. Accordingly, the new strategy states that re-engagement should be at the heart of each contact with taxpayers²⁴³ to help them understand and manage their payment obligations.²⁴⁴ It is also intended to minimise the risk of creating an uneven playing field by taking into account taxpayers' circumstances.²⁴⁵ Furthermore, the ATO plans to transform the culture of the DBL by shifting 'from a rules-based approach to one based on risks, outcomes and principles'²⁴⁶ which allows officers to exercise good judgment and consider the circumstances of the taxpayer to 'positively influence willing participation'.²⁴⁷
- 2.69 Furthermore, the earlier mentioned BRP and Analytics Projects have aspects which are aimed at reducing aged debt and improving the ATO's use of debt activities based on taxpayers' circumstances.²⁴⁸ For example, the BRP aims to determine, amongst other things:
- the impact of early interventions on compliance behaviour;

237 ATO, *Risk Management in the Enforcement of Lodgment Obligations and Debt Collection Activities*, PS LA 2011/6, 28 November 2013, paras [15], [31].

238 Michael D'Ascenzo, 'At Your Service: Here to Help and Look After the Interests of Business Making Good and Honest Choices (Council of Small Business of Australia - the NAB National Business Summit, Homebush, Sydney 27 July 2011).

239 Ibid.

240 ATO, 'Office Minute July 2014', above n 147; ATO, 'Debt Right Now', above n 145.

241 ATO, 'Office Minute September 2012', above n 144.

242 ATO, 'Office Minute July 2014', above n 147.

243 ATO, 'Debt Strategy 2014-18', above n 42.

244 ATO, Communication to the IGT, 7 October 2014; ATO, 'Service Delivery Plan', above n 168, pp 5-6.

245 ATO, 'Debt Strategy 2014-18', above n 42; ATO, 'Roadshow', above n 173, p 4.

246 ATO, 'Service Delivery Plan', above n 168, p 10.

247 Ibid; ATO, 'Debt Strategy 2014-18', above n 42.

248 ATO, Communication to the IGT, 11 September 2014; ATO, 'Roadshow', above n 173.

- sanctions which have the most or least impact on taxpayer behaviours and compliance;
 - any ‘tipping’ points where sanctions will dissuade payment of tax debts; and
 - incentives to pay on time or quickly address a default when it occurs.²⁴⁹
- 2.70 The ATO has advised that the Analytics Project’s Optimal Case Action Matching model (Optimiser model) is intended to determine the optimal time to take recovery action.²⁵⁰ The Analytics Project also aims to develop models which analyse the relationship between debt cases and treatment actions. These models will include:
- an Action Response Propensity model which identifies taxpayers that are most likely or most unlikely to respond to a given type of action; and
 - a Next Best Action model which uses other models to build a model that provides a recommendation for the best next action on each case.
- 2.71 In addition to the above work, the ATO has also sought to update its debt letters and scripting to incorporate behavioural economics principles and associated design improvements to positively influence voluntary compliance. The ATO recognised that taxpayer’s decisions are not always made on a rational basis and that it could be made easier for them to make the right choices by, for example, ensuring the consequences of non-compliance are clear and stated upfront and making it easier for taxpayers to understand the steps they need to take to address their debts.²⁵¹
- 2.72 For example, the following standard ATO letters to taxpayers were updated in line with behavioural economics principles:
- NILA letter;
 - Interactive Voice Response (IVR) letter; and
 - FAW letter.

²⁴⁹ ATO, ‘Attitudinal and Behavioural Research’, above n 192.

²⁵⁰ ATO, Communication to the IGT, 12 February 2015; ATO, ‘UTS project’ above n 197, p 2.

²⁵¹ OECD, ‘Tax Debt Management’, above n 45, p 44.

- 2.73 The ATO has tested the effectiveness of these changes. The updated IVR and FAW letters appear to have had a consistent but slightly positive influence on taxpayers.²⁵² However, the results were mixed for the updated NILA letter. For example, whilst activity statement debts paid in full increased slightly, the number of taxpayers who did not address such debts also slightly increased but the number of taxpayers entering into related payment arrangements decreased significantly. For income tax debts there was a slight increase in the number of taxpayers who only partially paid their debts, however, there was a rise in taxpayers whose debts increased and a reduction in taxpayers who entered into payment arrangements.²⁵³
- 2.74 Towards the end of this review, the ATO advised the IGT that it has recently begun updating its suite of debt letters to incorporate behavioural economics principles and to make the letters easier for taxpayers to understand.²⁵⁴ The ATO advice also indicates that the new letters are expected to be implemented in March 2015.²⁵⁵

IGT observations

- 2.75 It is commonly accepted that the longer a debt has been outstanding, the more likely that recovery activity will be unsuccessful. For example, the ATO has found that the probability of recovering debts after they have aged one year is approximately 2 per cent²⁵⁶ and the dividend from delayed ATO-initiated insolvency is significantly less than earlier action taken by other creditors.²⁵⁷ Therefore, early action may have a significant impact on the effectiveness of recovery activities. However, the manner in which the ATO pursues debt recovery should not jeopardise a taxpayer's ability to generate future income and economic contribution in ordinary circumstances. Accordingly, there is a difficult balance to strike between recovering tax debt efficiently and minimising risk to government revenue on the one hand and providing appropriate financial accommodation to the taxpayer on the other.
- 2.76 As mentioned above, the ATO has commenced research to improve upon the linear DRN strategy which includes better identifying taxpayers who would repay their debt without any ATO action, selecting the most effective actions for particular taxpayers and the optimal time for this action. The ATO expects the results of this research to assist in recovering debts earlier and be more proportionate to taxpayers' circumstances. The number of the ATO's research projects aimed at such improvements is a positive development and is consistent with the OECD's findings that revenue authorities need to be able to choose from a suite of interventions, ranging from soft measures through to firmer enforcement measures.²⁵⁸

252 ATO, 'Impact of Revised IVR Letter: An Examination of the Effect of Changing the IVR Letter' (Internal ATO document, 24 June 2014); ATO, 'Impact of Revised Firmer Action Warning Letter: An Examination of the Effect of Changing the Garnishee Warning Letter/Firmer Action Warning Letter' (Internal ATO document, 24 June 2014).

253 ATO, 'Impact of Revised NILA Letter: An Examination of the Effect of Changing the Notice of Intended Legal Action (NILA) Letter' (Internal ATO document, 24 June 2014).

254 ATO, Communication to the IGT, 26 February 2015.

255 ATO, Communication to the IGT, 1 April 2015.

256 ATO, Communication to the IGT, 11 December 2014.

257 ATO, Communication to the IGT 12 February 2015.

258 OECD, 'Tax Debt Management', above n 45, p 15.

- 2.77 An approach which is proportionate to taxpayers' circumstances also allows for more targeted interventions and efficient deployment of resources. However, the accurate identification of taxpayers' circumstances is not without challenges given the size and variation of the taxpayer base. Another risk for the new strategy is whether frontline staff can engage with taxpayers and make consistent decisions which are appropriate to individual circumstances. Accordingly, effective staff training, 'cultural support', decision making and capability development (an issue discussed further in Chapter 4) are also critical factors.
- 2.78 Achieving equity and fairness consistently and being perceived to be doing so is not a simple matter. For example, assisting insolvent taxpayers may seem generous but may also create a competitive advantage (effectively using unpaid tax debts as an unsecured source of finance to help them compete and fund growth or lifestyle²⁵⁹) and exacerbate the indebtedness to other creditors, thereby increasing the risk of broader economic harm. The ATO has to clearly and concisely communicate the reasons for its actions and how those actions are referable to taxpayers' particular circumstances to dispel perceptions of inequity. Indeed, some commentators have suggested that enforcement strategies that elicit feelings of resentment towards compliance and towards authority may lead to subsequent non-compliance.²⁶⁰ The challenge for the ATO will be to gain support for their strategies and minimise perceptions such as more aggressive pursuit of small businesses than large businesses.
- 2.79 The ATO has sought to improve its engagement with taxpayers through its research projects, including the updating and testing of its debt-related letters. However, before these research projects are concluded, it would be useful to see whether these projects should be expanded or modified based on experience of other revenue agencies such as research done by the IRD in New Zealand. The IRD had found that, to prevent new debts from aging and attracting penalties and interest, some taxpayers respond better to letters whilst others, particularly those with medium to high debts, respond better to phone calls. For the latter taxpayers, it was considered that phone calls provided them with an opportunity to interact with the IRD where they otherwise would not.²⁶¹ Similar findings could allow the ATO to take more proportionate interaction with taxpayers which could better encourage them to pay their debts.
- 2.80 It is acknowledged that the fruition of the ATO's research may take some time particularly if they are to be modified or expanded. Accordingly, the IGT believes the ATO should take some interim measures which, depending on their successes and the findings of the research, may be maintained in the longer term. Such measures should include taking earlier, more frequent and less intrusive follow-up action, such as fortnightly reminders, where taxpayers have not sought to address the tax debt in question. Such action could commence after the period of time, identified by the 'self finaliser' models, by which most taxpayers have paid their tax debt without any ATO promptings.

259 ATO, Communication to the IGT, 6 March 2015.

260 Kristina Murphy, 'Enforcing Tax Compliance: To Punish or Persuade?' (2008) 38(1) *Economic Analysis & Policy* 113, p 130.

261 OECD, 'Tax Debt Management', above n 45, p 71.

- 2.81 The above follow-up action has been generally supported by stakeholders and may avoid the necessity for firmer recovery action later. Such an approach would provide an environment more conducive to quicker repayment, resulting in better outcomes for both taxpayers and the ATO alike.

RECOMMENDATION 2.3

The IGT recommends that the ATO:

- (a) better inform the public about its debt strategy by, for example, publishing its approach to debt collection, including any changes or modifications thereto; and*
- (b) as an interim measure, whilst awaiting the result of its research projects, take earlier, more frequent and proportionate debt recovery action to minimise the necessity to take firmer action at a later time.*

ATO response: Agree

The ATO is rolling out an enhanced program of communication and collaboration with the community, intermediaries and our staff about our contemporary and tailored approach to debt collection.

As part of the shift in our approach to debt collection we will intervene earlier to prevent debts from escalating beyond control. This will be achieved through initiatives such as the Analytics for Client Engagement (ACE) program, which enables us to better understand the appropriate actions to take at the earliest point in time.

IMPACT OF ATO DEBT ACTIVITIES ON OTHER CREDITORS

- 2.82 Stakeholders have questioned the extent to which the ATO considers the impact of its debt recovery actions on other creditors. For example, as mentioned earlier, they have observed that the ATO may be providing financial accommodation to repeat debtors and insolvent taxpayers. In these situations, third party creditors are said to be unaware of such accommodation and are put at risk due to secrecy legislation preventing the ATO from disclosing tax debts publicly.
- 2.83 Stakeholders also consider that the ATO could play a greater role in prompting unviable businesses to address their debts and ameliorate the impact on other creditors because:
- the ATO is normally the main creditor in insolvency actions;
 - the ATO is the ‘canary in the coal mine’ as the business is required to report financial information to the ATO and that information is not available to other creditors;
 - it is relatively expensive for other creditors to take insolvency action against debtors and withholding supply of goods and services is generally a more cost effective means to obtain payment; and

- it is easier for the ATO to take action than other creditors or ASIC as the ATO has significant powers to focus a company's attention on its financial obligations, such as through DPNs and garnishee notices as well as not being required to prove a debt before taking recovery action.
- 2.84 In taking debt recovery actions, certain stakeholders have advised that creditors often rely on the ATO to take quick and appropriate action in relation to insolvent taxpayers. Furthermore, to better consider the impact of debts on creditors, they believe that the ATO should focus debt recovery activities on certain industries, particularly the building, construction and labour hire industries. These industries are considered by these stakeholders to be more prone to phoenix activity and non-lodgment which can mask tax debts, hide assets and adversely impact all creditors, including the ATO. They also believe that phoenix activity may be better addressed if the interaction between the ATO and other agencies, such as ASIC were less sporadic.

ATO materials

- 2.85 The ATO has advised that insolvency has a propagating impact through the economy as approximately one-third of insolvencies are caused by debtors being unable to pay their creditors. To help address this problem, the ATO has engaged private sector consultants and a professional body to develop a pre-insolvency framework. The framework is expected to identify formal actions that the ATO could take to prevent debts from arising or turnaround businesses.
- 2.86 In addition to the pre-insolvency framework, the ATO also uses the BVAT and has piloted optional IVAs conducted by a third party assessor as mentioned in Chapter 1. Both the BVAT and IVAs are aimed to test businesses' viability before proceeding with insolvency action so that non-viable businesses are more accurately identified. For example, in one IVA, a \$9 million debt was repaid within a 24 month payment plan due to business restructuring advice that enabled the company to avoid winding up.²⁶²
- 2.87 In relation to insolvency, particularly as a result of phoenix activities, the ATO is a member of the Inter-agency Phoenix Forum²⁶³ which aims to assist in delivering government commitments to address such activities. The forum aims to share intelligence between agencies in a timely manner and encourage agencies to focus jointly on the worst phoenix operators.²⁶⁴
- 2.88 The forum has two broad roles, namely:
- an intelligence advisory role by reviewing intelligence reports from agencies and ensuring all agencies harvest available intelligence; and

²⁶² ATO, 'IVA Pilot Evaluation', above n 162, p 4.

²⁶³ ATO, 'Service Delivery Plan', above n 168, p 20.

²⁶⁴ ATO, *Inter-agency Phoenix Forum: Purpose* (2014) <<https://www.ato.gov.au>>.

- a strategic oversight advisory role which includes promoting cross-agency understanding of agency powers and constraints, minimising inefficiencies between agencies as well as collaboration for early identification and management of phoenix cases supporting the best mix of treatments.²⁶⁵
- 2.89 The ATO has advised that the extent of information that could be disclosed by each agency was limited by the relevant legislation²⁶⁶. A new regulation has recently taken effect which prescribes a 'Phoenix Task Force' and 'Trust Task Force' which enables broader disclosures. For example, the new regulation will allow the ATO to act as a 'clearing house' to collate and disseminate information to other agencies. The agencies will also be able to jointly look at information and investigate clusters of risks or particular industries, such as the fruit picking industry in South Australia.²⁶⁷
- 2.90 Another Government plan to help reduce the impact of phoenix activities is the establishment of a 'phoenix watch list' to be incorporated into the Australian Business Register which also facilitates the sharing of information.²⁶⁸ The phoenix watch list commenced operation in January 2015.²⁶⁹
- 2.91 As the phoenix risk manifests itself in different tax contexts, various business lines within the ATO may become involved, each having a separate risk treatment plan.²⁷⁰ Essentially, there is no single phoenix population. Towards the end of this review, ATO management made representations to the IGT that a single 'phoenix risk population' had recently been identified to determine the proportion of debts attributable to phoenix activity.²⁷¹

IGT observations

- 2.92 Insolvency has a propagating impact through the economy and can result in the insolvency of others. As mentioned in Chapter 1, in a D&B survey, 34 per cent of businesses stated that late payments interrupt their cash flow and operating costs, resulting in delays in paying their suppliers.²⁷²
- 2.93 In insolvency cases, 89 per cent of debts are irrecoverable²⁷³ and therefore the cash flows and viability of creditors are significantly affected. Practical application of the insolvency rules heavily relies on creditors to initiate proceedings. However, creditors may be unaware of commercially sensitive financial difficulties experienced by its debtors particularly where they are paid promptly in preference to other creditors. This suggests that insolvent trading may often remain undetected.

²⁶⁵ Ibid.

²⁶⁶ For example, the ATO could only disclose certain information to ASIC if it related to a breach of the *Superannuation Industry (Supervision) Act 1993* provisions with criminal or civil liability.

²⁶⁷ ATO, Communication to the IGT, 10 December 2014.

²⁶⁸ Ibid; ATO, *Inter-Agency Phoenix Forum Minutes* (24 July 2013) <<https://www.ato.gov.au>>.

²⁶⁹ ATO, Communication to the IGT, 1 April 2015.

²⁷⁰ Various tax obligations which may be impacted by phoenix activities are managed by different business lines. For example, PAYG Withholding and debt obligations are managed by the Debt and SBIT business lines, super guarantee obligations are managed by the SBIT and Superannuation business lines and indirect tax obligations are managed by the Indirect Tax business line.

²⁷¹ ATO, Communication to the IGT, 1 April 2015.

²⁷² Dun and Bradstreet, above n 3.

²⁷³ ASIC, 'Report 372', above n 2, p 7.

- 2.94 In the IGT's view, the ATO is in a generally stronger position to address insolvencies compared to other creditors and government agencies. The ATO has access to vast amounts of financial information which other creditors and agencies do not. Furthermore, the ATO is likely to be the most common creditor in all insolvencies due to the near universality of tax obligations. Indeed, it could be argued that the efficiency and effectiveness of the insolvency system relies significantly on the ATO to take appropriate action.
- 2.95 It is a difficult task to determine whether a taxpayer needs time to trade out of debt or whether the taxpayer is headed for insolvency or is otherwise trading as a going concern. As will be discussed in Chapters 3 and 4, improving the ATO's ability to determine credit risk should assist the ATO in this respect. Importantly, such an improved ability also allows the ATO to utilise the BVAT and other tools at an earlier point in time to encourage taxpayers to seek professional advice and consider voluntary administration as well as providing incentives to do so where appropriate. Such ability would also minimise the need for unnecessary legal enforcement.
- 2.96 Furthermore, taxpayers, their advisers and third party assessors, who were involved with the pilot of IVAs, have commented favourably on the pilot. Accordingly, the IGT believes that a cheaper and less intensive IVA could be useful in providing assistance to those smaller businesses with larger business debts, particularly where there is disagreement as to the business' viability.
- 2.97 Although the ATO may provide payment assistance to businesses, such action is not without risks to other business creditors. For example, unlike commercial debts, tax debts are invisible to other creditors until the ATO takes firmer recovery action. Accordingly, where the ATO provides payment assistance to a business with uncertain viability, it may expose other creditors to the risk of greater economic harm as they are unaware of the business' financial difficulties.
- 2.98 However, it is unclear whether the ATO's new RDF-based debt management strategy and ACE program adequately considers the potential impact of debts, insolvency and payment assistance on other creditors. The IGT believes that the ATO's strategy could be improved if the strategy included these potential impacts, particularly as it has a role to act in the best interests of the broader economy and not only in relation to the taxpayer in question.
- 2.99 Another initiative suggested by a few stakeholders is that if the ATO is unable to take sufficient action against insolvent taxpayers, the ATO could release information to the public. Some revenue authorities publish the names of debtors, such as in Korea and Sweden. The Korean approach is to publish debtors' information once their debts reach a certain threshold. Sweden on the other hand, fundamentally believes that debtors information should be made public, thus anyone can request the debt information of another which can also be used by credit rating agencies.²⁷⁴ Whilst there are cultural differences which may make the Swedish approach less viable in Australia, it has been suggested that a similar approach to that of Korea may be more suitable. Regardless of the merits of each approach, the publication of such information would require legislative change to the ATO's secrecy requirements.

274 OECD, 'Tax Debt Management', above n 45, p 55.

- 2.100 The IGT is of the view that similar outcomes to the above may be achieved by the 'phoenix watch list'. Once the relevant legislation is passed, it will allow the ATO to act as clearing house' to collate and disseminate information to other agencies. The freer flow of information would better support the operation of the watch list and provide useful information to the market, particularly given the far-reaching impacts of insolvency.
- 2.101 More specific to phoenix activities, research conducted by the Australian Securities Commission (ASIC's predecessor) in 1996 found that 80 per cent of respondents who had experienced phoenix activities did not report it to the authorities.²⁷⁵ Deliberate phoenix activity not only reduces government revenue but also adversely affects others, including business employees and other creditors.
- 2.102 The ATO has advised that some phoenix activities are the result of careful planning and assistance from legal and insolvency professionals. However, phoenix activities may also be the result of opportunistic behaviour by some financially distressed owners. Therefore, in addition to targeting phoenix activity in specific industries, many stakeholders believe an education program could be run to help small business owners and other directors, who may invariably be family members or silent directors, become aware of their legal responsibilities. Indeed, there are no formal qualifications required to start a business (for example, receive an Australian Business Number or ABN). Whilst the ATO has commenced work with ASIC and state revenue agencies to provide information on the director penalty regime via each agency's website, the ATO could also consider working with other agencies, such as the ABSC to jointly develop a more integrated suite of materials on a broader range of issues for small business owners. These materials could then be made available on each agency's website, on the provision of an ABN and further promoted at other appropriate times. Such education could also form part of the proposed new ATO treatment plan for phoenix activities.
- 2.103 As noted earlier, each business line within the ATO had their own approach and plan for dealing with phoenix activity and, during the review, planned to develop an integrated strategy. Stakeholders have also supported better strategic integration to deal with phoenix activity. The IGT believes that a coherent and integrated strategy to deal with phoenix activity could result in more informed and consistent actions being taken across the ATO and allow better assessment of the effectiveness of those actions. The new strategy should also take into account the proposed regulations to ensure the best use is made of the new powers contained within them. Furthermore, as some phoenix activity requires the assistance of advisers, the new phoenix strategy should include engagement with intermediaries which may interact with different areas of the ATO and not just those which address phoenix activities.

²⁷⁵ ASC, *Phoenix Companies and Insolvent Trading* (Research Paper No. 95/01, July 1996) pp 2-5.

RECOMMENDATION 2.4

The IGT recommends that the ATO:

- (a) jointly develop with other relevant agencies, a suite of educative materials for small business owners on their legal responsibilities; and*
- (b) continue to implement and refine the integrated risk treatment plan, for phoenix activity across the organisation, which incorporates the new inter-agency powers, engagement with intermediaries and assessment tools for measuring the success of the plan.*

ATO response: Agree

In relation to sub-point (a) the ATO agrees to this recommendation recognising that successful progress is contingent on other agencies' commitment to achieving the recommended outcome. We currently have a cross-government program of work to provide information to small business owners on their legal responsibilities – known as the Fix-it-Squad. The Fix-It-Squad process includes the engagement of small business representatives and intermediaries to identify areas of focus and co-design an improved experience outcome, and to-date has delivered:

- A guide for small business directors published on ASIC's Small Business Hub (www.asic.gov.au/small-business); and
- New content on www.business.gov.au to help small business owners make informed decisions about which business structure is best for them.

In relation to sub-point (b) the ATO will continue to review and improve its Phoenix strategy, noting its progress in this area, which includes:

- the allocation of 2015-16 Federal Budget funding for a new Serious Financial Crime Taskforce, to focus on phoenix operators, and intermediaries / facilitators of financial crimes
- establishing a single 'phoenix risk population' to determine the proportion of debts attributable to phoenix activity and to identify the connected individuals involved with potential phoenix operations
- establishing and chairing the Inter-agency Phoenix Forum, which utilises the regulation / legislative instrument prescribing an information sharing Taskforce. Through this Forum, the ATO has led the development and implementation of a whole-of-Government communication strategy on phoenix risk
- establishing a Phoenix Watch-list contributed to by the ATO and several State Revenue Offices.

PUBLIC REPORTING OF TAX DEBTS

2.104 Stakeholders have raised concerns regarding the ATO's public reporting of tax debts and its related activities. These concerns were in relation to the level, timing, age, composition and transparency of reporting. Stakeholders believe that more detailed reporting could also be used to better inform the ATO on which areas could be targeted to more effectively address tax debts and identify impact on the economy and taxpayer behaviours.

ATO materials

2.105 The ATO publicly reports a break up of its debt holdings in the Commissioner's Annual Report. For the 2013–14 year, the following was reported:

- the proportion of tax liabilities paid by the due date broken down into PAYG withholding, individuals' income tax (returns and instalments), companies' income tax (returns and instalments), GST and excise;
- gross and net tax collections;
- debts attributable to ATO compliance activities, including interest and penalties;
- the 'collectability' of debts, including whether debts are disputed or where taxpayers become insolvent (irrecoverable at law);
- a break up of 'collectable' debts by income tax, activity statement and superannuation guarantee debts as well as the largest taxpayer segment contributing to collectable debts;
- provisions for 'bad and doubtful debts' and remissions; and
- the cost of collection (per \$100) as well as the increase in amounts collected attributable to ATO action and collections per full-time equivalent staff.²⁷⁶

2.106 The ATO's reported statistics are set out and analysed in Chapter 1. It should be noted that in the 2012–13 Annual Report, in relation to the collectability of debts, the ATO also separately accounted for debts which were treated as uneconomic to pursue. However, in other recent years, these amounts were combined with amounts that were irrecoverable at law.²⁷⁷

2.107 In addition to the above publicly reported statistics, the ATO also maintains a range of internal statistics, which were also reproduced and analysed in Chapter 1, and a range of metrics which include:

- 'Inventory turnover ratio' which indicates how quickly the ATO recovers debt;
- 'Resolution of New intake' measures how quickly the ATO is collecting new debt within the year; and

²⁷⁶ Commissioner of Taxation, 'Annual Report 2013-14', above n 35, pp 10, 14, 17, 40-41, 45-47, 50, 88.

²⁷⁷ Commissioner of Taxation, *Annual Report 2012-13* (2013) p 35.

- ‘Roll rate’ which indicates how well the ATO stops debts from aging and growing.²⁷⁸

2.108 During the review, the ATO has advised that it is aiming to realign its metrics with the OECD’s principles²⁷⁹ to also measure the ATO’s effectiveness of changing taxpayer behaviours to prevent debts from arising and making it easier for taxpayers to comply. Once fully developed and implemented, the ATO believes that these metrics should allow it to more effectively measure payment ‘on time’ and payment ‘over time’.²⁸⁰ The draft effectiveness measures are reproduced in Appendix 6.

IGT observations

- 2.109 KPIs are essential to measure the performance of the debt collection function as a whole and more particularly the measurement of outcomes at the strategic, operational and individual level. As noted by the OECD, in addition to setting overarching targets to align the daily operations of the collection function with desired outcomes, KPIs can also be used to identify potential improvements and lead to the development of improvement initiatives. To achieve these aims, the correct performance indicators are essential.²⁸¹
- 2.110 Public reporting and analysis of the composition and nature of taxation debts benefits both the ATO and community as it enables greater transparency and confidence that key risk areas are identified and being addressed by the ATO. The IGT considers the ATO’s plans to improve its debt metrics is encouraging.
- 2.111 The ATO’s current published statistics provides transparency with respect to the main areas in relation to tax debts, such as the levels and composition of the debts. However, greater focus on key areas would assist community understanding and engender greater support for the ATO in terms of its strategies to effectively address the main contributors to tax debts.
- 2.112 The ATO has further statistics which are only available internally.²⁸² These could better assist community understanding if they were made publically available. For example, as presented in Chapter 1, most collectable debt is owed by micro businesses with respect to activity statement amounts which are aged less than six months. Such information could assist in explaining why the ATO may choose to take some action to particularly assist taxpayers in this market segment meet their tax obligation.

278 ATO, Communication to the IGT, 11 December 2014; ATO, ‘PBS Measures’ (Internal ATO document, April 2014).

279 OECD, ‘Tax Debt Management’, above n 45.

280 ATO, ‘Measuring Performance in Payment Compliance Workshop’ (Internal ATO document, November 2014); ATO, Communication to the IGT, 27 February 2015.

281 OECD, ‘Tax Debt Management’, above n 45, pp 16, 79-80.

282 ATO, Communication to the IGT, 11 December 2014.

- 2.113 The IGT also believes that the ATO could also undertake further statistical analysis to better inform the public, as well as itself, and appreciate the causes of tax debt or why debt has increased consistently since 2003 (including as a proportion of GDP) despite the ATO's earlier debt strategies. For example, whilst the ATO currently measures whether payment of debt has been the result of self-assessment or due to compliance activities. More refined metrics in relation to payment 'on time' could indicate the connection of payment to the quality of compliance activities and whether there is a need for a greater focus on having a payment discussion with the taxpayer as the compliance activity is being finalised. This would potentially result in the taxpayer, particularly micro businesses, being more aware of their financial situation and payment options at an earlier stage.
- 2.114 Whilst payment on time is important, ensuring that taxpayers' maintain good longer term payment behaviours is also important so that any earlier ATO efforts are not wasted and taxpayers again fall into arrears. Supporting good longer term payment behaviours will help prevent taxpayers from incurring debts in future and the need for further ATO intervention. Accordingly, the ATO should also measure the impact of its activities on longer term payment behaviours to determine the effectiveness of the actions it has taken. For example, such a measure could identify where debts are attributable to first-time debtors or serial debtors, including escalating and compounding amounts.
- 2.115 The above metrics could also be further refined in future to identify the events that give rise to different types of tax debts and how the ATO can better influence taxpayer behaviours and attitudes to both pay on time as well as 'over time'. Having a better understanding of why and when people are motivated to comply with payment obligations can provide the ATO with more effective strategies.
- 2.116 Measuring these amounts would help the ATO to improve its debt collection strategies and reporting them would allow the community to understand the benefit of the ATO's actions for the broader economy. Such measurement could be undertaken by the ATO's Revenue Analysis Branch which is responsible for development of effectiveness indicators as well as advice on the measurement of compliance and the effectiveness of revenue collection administration amongst other things.²⁸³

283 ATO, Communication to the IGT, 27 February 2015.

RECOMMENDATION 2.5

The IGT recommends that the ATO:

- (a) publish further statistical information and analysis, currently only available internally, to better inform the public about tax debt and strategies to address them; and*
- (b) undertake further statistical analysis to develop improved metrics, which are reported publically, to better describe the effectiveness of its debt strategies in relation to such issues as improving payment on time, payment behaviour over the longer term and the benefit to the economy.*

ATO response: Agree

The ATO commits to publishing additional information on the level of debt and effectiveness of the ATO's debt management strategies, and notes a range of information and analysis is published each year in the Commissioner of Taxation's annual report.

The ATO has reframed its outcome framework to align with the OECD outcomes of tax compliance. As part of the annual ATO corporate planning cycle all measures are reviewed in line with the outcome framework. We have recently undertaken a review of our debt measures and are committed to ongoing improvement in measuring the effectiveness of our debt management strategies and transparency in reporting.

CHAPTER 3 – ATO DEBT PAYMENT ASSISTANCE

- 3.1 Some taxpayers may experience cash flow difficulties that prevent them from paying their tax liabilities on time. In these circumstances, as an alternative to taking formal recovery action, the ATO may consider requests to accept payment of the debt by instalments over a period of time. Such ‘payment arrangements’ will ordinarily attract GIC until the liabilities are fully paid.²⁸⁴ As described in Chapter 1, the ATO largely determines whether to accept payment arrangements based on a taxpayer’s propensity and capacity to pay.
- 3.2 Other assistance that the ATO may consider, includes releasing taxpayers from their liabilities where they may suffer serious financial hardship or remit interest in appropriate circumstances.

SUMMARY OF STAKEHOLDER CONCERNS

- 3.3 Stakeholders have raised a range of concerns in relation to the ATO’s debt payment assistance. These are described under appropriate headings below.

PAYMENT ARRANGEMENTS

- 3.4 Stakeholders have raised many concerns regarding how the ATO determines whether to offer payment arrangements and the terms of those arrangements. An underlying theme seems to be that most ATO officers do not have sufficient capability to analyse the commercial viability of businesses and their particular circumstances, causing delays in negotiating payment arrangements.
- 3.5 Examples cited by stakeholders include those where ATO officers do not understand that financial information may be historical, whilst, when considering predictors of future capacity to pay, such as projected cash flows, management decisions and economic conditions, they do so without understanding that different industries have different margins and cash flows. For these reasons, stakeholders have questioned the level of training and development of ATO officers working in debt management and the veracity of the tools which support them.
- 3.6 Specifically, whilst stakeholders consider such tools, like the BVAT, useful to assist ATO officers, these should only be used as a starting point and not followed too rigidly given that there is no single discrete indicator of viability. Accordingly, over reliance on such tools to determine the ATO’s approach is considered to be inappropriate.

²⁸⁴ ATO, ‘General Debt Collection Powers and Principles’ above n 48, paras [52]-[54].

- 3.7 Stakeholders have also observed that the ATO will not discuss or enter into payment arrangements:
- with certain taxpayers, including those who are unemployed;
 - in certain circumstances, such as where a company was defrauded by an employee resulting in uncertain superannuation entitlement; and
 - despite ATO requirements being met, such as where taxpayers have lodgments up-to-date.
- 3.8 Whilst stakeholders recognise that the ATO should not offer payment arrangements to taxpayers with no likely future capacity to pay, in a number of examples provided in submissions to this review, the taxpayers could pay their debts. In these cases, stakeholders have asserted that the ATO was being uncooperative and only through escalating matters were arrangements agreed and subsequently paid in full. Stakeholders are concerned that where payment arrangements are refused, the only alternative is insolvency proceedings. Stakeholders say this outcome is not efficient and that the ATO should work with taxpayers to come to an arrangement, particularly as bankruptcies do not result in many sequestration orders which implies that the debts were ultimately paid.
- 3.9 Stakeholders also believe that ATO information requests from taxpayers to prove capacity to pay when negotiating payment arrangements adds to taxpayers' costs which causes additional financial strain. A number of stakeholders commented that the ATO should accept taxpayers' proposed arrangements at face value. Their adherence to the arrangement would be sufficient proof of their capacity to pay.
- 3.10 Furthermore, stakeholders consider that the ATO intimidates taxpayers into unaffordable payment arrangements despite BVAT indications of the unaffordability of such payments. For example, stakeholders have observed that the ATO commonly pressures taxpayers to make a 50 per cent upfront payment with short payment timeframes for the remainder of the tax debt.
- 3.11 Accordingly, stakeholders have commented that the ATO needs to be more flexible, better consider taxpayers' circumstances and the consequences of future debts arising. Some taxpayers are believed to agree to the ATO's terms even though they cannot afford the payments and do not appreciate the consequences. For example, when unaffordable arrangements are later renegotiated, the ATO considers this to be a 'default' which makes it difficult for taxpayers to enter into arrangements in future.
- 3.12 Stakeholders have further asserted that ATO officers do not appear to have a consistent approach to offering payment arrangements to taxpayers with similar circumstances. An often made comment was that it appeared to be dependent on the ATO officer you get on the day. For example, in one case a tax agent was unable to secure their client a payment arrangement but the client succeeded when they contacted the ATO directly.

- 3.13 Stakeholders also considered that while not wide-spread, ATO officers have sometimes engaged in inappropriate behaviour, for example being overly aggressive, delaying communications or asking tax agents to guarantee their clients' payment arrangements.
- 3.14 For the reasons above, stakeholders have questioned the nature of the ATO's procedures, whether ATO officers are following those procedures and the need for better staff guidelines and training.
- 3.15 Stakeholders have also raised some constructive examples where officers were understanding and made payment arrangement more affordable as long the debt was being reduced and taxpayers were paying on time. Stakeholders also appreciate the ATO's automated payment arrangement phone line for debts less than \$25,000.

ATO materials

- 3.16 The Commissioner is not obliged to accept payment arrangements and makes such decisions based on risk, for example, a taxpayer's propensity and capacity to pay²⁸⁵ as well as their individual circumstances.²⁸⁶ As part of this risk analysis, if the prospects of recovery in the longer term would be diminished or the revenue would be disadvantaged, payment arrangements will not be accepted.²⁸⁷ To this end, the ATO may request information from a taxpayer to support their application for a payment arrangement.²⁸⁸
- 3.17 The range of factors considered by the ATO and the determination of capacity to pay (for example, via the BVAT) in deciding whether to accept a payment arrangement were described in Chapter 1. However, the use of the BVAT is only required where debts exceed \$50,000 and where the proposed payment arrangement does not align with the ATO's risk assessment of the case.²⁸⁹ Where it is determined that a business is not viable or that an individual does not have capacity to pay, payment arrangements will not be accepted by the ATO and formal recovery action may commence.²⁹⁰
- 3.18 The ATO has advised that it does not have effectiveness measures for the BVAT, such as in relation to the sustainability of payment arrangements, as the tool only supports officers' judgment. However, the ATO has advised that 57.46 per cent of pre-BVAT arrangements were defaulted as opposed to 28.17 per cent of arrangements post-BVAT. Similarly the pre-BVAT arrangements had a 'cancellation rate' of 23.85 per cent as opposed to 17.57 per cent of post-BVAT arrangements.²⁹¹

285 ATO, Communication to the IGT, 7 October 2014.

286 ATO, 'General Debt Collection Powers and Principles' above n 48, para [56].

287 Ibid, para [63].

288 Ibid, paras [59], [63].

289 ATO, 'BVAT Parameters' above n 158; ATO, 'DRN Company Matrix', above n 53.

290 ATO, Communication to the IGT, 8 January 2015.

291 Ibid.

- 3.19 Towards the end of the review ATO management made representations to the IGT that a new Payment Arrangement Criteria Assessment Tool had been developed. They have indicated that this tool was based on analytical research and predictive modelling and would identify a given taxpayer who presents a high risk of not reducing their debt by a certain threshold. The tool is intended to assist ATO officers in deciding whether to grant payment arrangements to such high risk taxpayers.²⁹²
- 3.20 Where payment arrangements are determined to be appropriate, taxpayers are requested to make an upfront payment and finalise their debts in the shortest possible timeframe. If the ATO has concerns about the solvency of taxpayers or their ability to meet the payment terms proposed, taxpayers may be required to provide security.²⁹³
- 3.21 The ATO's DBL and Customer Services and Support Business Line (CS&S) officers which handle 'inbound requests'²⁹⁴ may enter into payment arrangements within the level of authorisation which was outlined in Chapter 1. The ATO has advised that it has formal training for DBL staff which includes induction, risk assessment, negotiation and financial statement training.²⁹⁵ The ATO expects this training, in conjunction with its relevant procedures, would assist staff, actioning lower risk cases, to enter into sustainable payment arrangements.²⁹⁶
- 3.22 For staff actioning higher risk cases, as mentioned in Chapter 1, the ATO has mandatory training on the use of the BVAT and conducted voluntary refresher training during the review. In total, 114 staff had attended the refresher training at the time of writing this report.²⁹⁷
- 3.23 During the review, the ATO also developed a tool for DBL staff to identify the number of payment arrangements which they have agreed including those that were defaulted by the taxpayer. The ATO has advised that this tool will help team leaders to identify and address skilling needs.²⁹⁸
- 3.24 A private sector secondee to the ATO, however, observed that there did not appear to be any formal training programs for new ATO staff and that investigation of taxpayers' circumstances and analysis of their payment proposals were often overlooked even by more experienced debt staff who had demonstrated a limited capability to review payment proposals and financial statements.²⁹⁹

²⁹² ATO, Communication to the IGT, 1 April 2015.

²⁹³ ATO, 'General Debt Collection Powers and Principles' above n 48, paras [63]-[64].

²⁹⁴ ATO, Communication to the IGT, 12 December 2014; ATO, Communication to the IGT, 21 January 2015.

²⁹⁵ ATO, 'Standard Training Schedule - Early Collections' (Internal ATO document, July 2014), ATO, 'Standard Training Schedule - Firmer Action', above n 160, ATO, 'Standard Training Schedule - Strategic Recovery, Superannuation, Large & Consolidated (SRS)' (Internal ATO document, July 2014), ATO, 'Learning and Development - Toolkit' (Internal ATO document, undated), ATO, 'Debt Skill Set - Work Activities', above n 160; ATO, 'Payment Arrangements - Overview Learner Workbook' (Internal ATO document, July 2012).

²⁹⁶ ATO, Communication to the IGT, 28 April 2015.

²⁹⁷ ATO, Communication to the IGT, 2 March 2015; ATO, Communication to the IGT, 1 April 2015.

²⁹⁸ ATO, Communication to the IGT, 1 April 2015.

²⁹⁹ An External Report.

3.25 Furthermore, the secondee observed that some debt staff were not making use of all the tools made available to them such as the BVAT. Some debt staff who did use the tool, however, did not fully understand the output produced by the tool and were unsure why the tool had produced particular results.³⁰⁰ Feedback received by the ATO's Debt Ministerial and Complaints unit also identified a number of cases where, for relatively small debts, payment arrangements had been refused. The ATO advises that it is considering modifying the scripting to enable officers to be less rigid in conversations with taxpayers with small debt.³⁰¹ As a result of this and other feedback sources, the payment arrangement conversation guidelines have been consolidated so that a taxpayer is given the same consideration regardless of whether they interact with DBL or CS&S staff.³⁰²

IGT observations

- 3.26 The IGT considers that many stakeholder concerns could be addressed through improved structured training and guidance materials as well as improved support tools provided to ATO officers to ensure that they make appropriate decisions in relation to determining payment arrangements.
- 3.27 The key capabilities in determining whether a payment arrangement should be entered and the terms of those arrangements are:
- commercial awareness to understand how businesses and particular industries operate; and
 - credit risk assessment (for example, analysis of taxpayers' management expertise, leverage and liquidity as well as the consequences of default and collection) based on financial information and which takes into account taxpayers' circumstances.
- 3.28 The ability of ATO officers to enter into appropriate payment arrangements is important as there can be many adverse consequences for taxpayers. For example, it may create undue financial pressures for taxpayers, result in their unnecessary insolvency, impact their ability to access ATO assistance in the future if they default or adversely impact their long-term voluntary co-operation if they feel unfairly treated. Conversely, arrangements may also be entered in inappropriate circumstances which give taxpayers an unfair advantage over competitors who do not require assistance as it may effectively fund growth in circumstances where the taxpayer would otherwise be required to seek credit. Accordingly, attuned judgment is required to ensure that the ATO recovers debts which are properly due and payable in a manner that benefits the economy.

³⁰⁰ Ibid.

³⁰¹ ATO, Communication to the IGT, 18 November 2014.

³⁰² Ibid.

- 3.29 The above ATO officer capability can be developed through formal structured training and consistent on-the-job supervision. The ATO currently has induction training for all debt staff which includes basic financial awareness of income, expenses, assets and liabilities. It is also in the process of updating its coaching framework for DBL staff.
- 3.30 To better align its capability with its overarching strategy, the IGT believes that the ATO should expand its new training framework to also focus on improving commercial awareness, taking into account taxpayers' circumstances and behaviours. The important behavioural elements include day-to-day aspects of business activities such as drawing on capital, extending payment timeframes to creditors and reducing payment timeframes for debtors. The level and extent of such training may need to incorporate specific needs and vary according to the type of work performed. Additionally, it is important that such training is kept up to date to ensure that staff do not lose these skills over time, particularly, if they are not used frequently.
- 3.31 It is also important that the experience of more senior officers is appropriately captured and disseminated to more junior staff. Whilst some ATO teams have a 'buddying' system, which will be more fully described in Chapter 4, the IGT notes that such buddying may be limited. The ATO's rule of thumb is that buddying should be one-third of the time taken in training, for example where a training program has a duration of 90 minutes, buddying is expected to be 30 minutes.³⁰³
- 3.32 The ATO also supports officers to make appropriate decisions by providing them with a range of tools. However, there are a number of issues in relation to these tools. First, the use of such tools is not mandated in all cases. Whilst this may be an appropriate requirement as collating information is expensive for both taxpayers and the ATO, more streamlined viability and capacity to pay tools may provide high level guidance on whether payment arrangements and their terms would be suitable. A streamlined tool would also minimise costs involved for both taxpayers and the ATO in collating and processing information. During the review, the ATO had commenced planning to develop a streamlined version of the BVAT for taxpayers. This could also be used by internal staff for lower risk cases. However, the full BVAT assessment should remain available in higher risk cases. In this respect, improved staff commercial awareness and credit risk assessment would allow more targeted information requests to be made which could similarly reduce costs.
- 3.33 The ATO is aware that there is room to further improve its officers' capability to determine a business' viability as well as use of supporting tools, such as the BVAT and their understanding of the outputs. There are indications that some debt staff are not making use of the tools available for analysing financial information, whilst others, who did use the tools, did not fully understand the tools' outputs.³⁰⁴ Although, it is also important that over-reliance is not placed on these tools, a better assurance system is needed to ensure that officers are following processes and making appropriate decisions (more fully discussed in Chapter 4).

303 ATO, Communication to the IGT, 19 November 2014; ATO, Communication to the IGT, 9 December 2014; ATO, 'Debt Skill Set Model' (Internal ATO document, undated).

304 An External Report.

- 3.34 The IGT believes that developing better commercial awareness and credit risk assessment capability would encourage officers to use the BVAT and encourage the use of the output of such tools to have more targeted discussions with the taxpayer. Where concerns remain with a taxpayer's capacity to pay, rather than declining to enter into a payment arrangement, officers could ask the taxpayer to provide a plan on how they intend to pay their debt and upcoming liabilities or submit to a lower cost independent viability assessment. This would allow the ATO to better consider the appropriateness of entering into payment arrangements with the taxpayers and avoid unnecessary costs and frustration for taxpayers.
- 3.35 The ATO could also tailor the BVAT outcomes based on particular industries where this information is readily available. For example, the IGT is aware that the ATO benchmarks a number of cash economy industries. Such information could be used to more accurately determine business viability within particular industries.
- 3.36 It is also understandable that staff may be confused by debt strategies and procedures which encourage the securing of a large upfront payment as well as short timeframes when negotiating arrangements. Such requirements may possibly result in ATO officers pressuring taxpayers into unmanageable payment arrangements without fully considering their circumstances. Whilst taxpayers should be encouraged to pay their debts quickly, it should be an achievable aim in their circumstances. This needs to be better communicated to debt staff, particularly as the private sector secondee has observed that whilst the ATO has taken positive steps towards a new debt strategy, some officers have not entirely come to terms with the strategy and revert back to the previous mindset and have taken enforcement action where it was perhaps not appropriate.³⁰⁵ Improving capability will also ensure that ATO staff appreciate taxpayer circumstances in deciding the terms of payment arrangements.
- 3.37 Furthermore, the ATO does not focus on ensuring consistency of decisions between various teams. A difficulty that ATO staff face is that they may have limited access to previous quality decisions and precedents. Without access to such materials, ATO officers may be tempted to form their own perceptions of good decisions. This issue will be more fully discussed in Chapter 4.
- 3.38 The IGT considers that the capture and dissemination of good payment arrangement decisions and associated reasoning would be invaluable to ATO officers. Such dissemination of corporate knowledge would assist staff to elicit principles which guide them towards better and consistent decision making. This can be achieved through the creation of a searchable database which includes precedents.
- 3.39 The IGT believes that appropriate supervision of staff would help ensure that they engage in a timely and appropriate manner and that requests are not unreasonable or made arbitrarily. The ATO has recently developed and commenced training for staff on negotiation with taxpayers which may also assist to alleviate stakeholder concerns if it also includes training on appropriate behaviours whilst attempting to secure the payment of debts. This training has been incorporated into induction packages for new staff undertaking debt-related work. Training and supervision will be further discussed in Chapter 4.

305 Ibid.

RECOMMENDATION 3.1

The IGT recommends the ATO:

- (a) expand its new training framework to include programs aimed at improving the commercial awareness and understanding of taxpayer behaviours for those staff who make decisions with respect to payment arrangements; and*
- (b) develop streamlined viability and capacity to pay tools which incorporate industry benchmarks for use in lower risk debt cases.*

ATO response: Agree in Part

The ATO agrees to (a) as our Reinvention blueprint intent is to build a professional and flexible workforce with the right skills, knowledge, attitude and tools to deliver excellent client service in a collaborative, supported and trusted environment.

To date, our program of work has included a focus on professional debt collection, business performance and viability, behavioural insights, and excellence in client service (including natural conversations). We have invited members of the community and intermediaries to talk with our staff, to expand our knowledge of business operations, obtain feedback on our service and products, and insights into how we can improve (putting ourselves in the shoes of our clients).

The ATO disagrees with (b). In our high volume, low risk environment the use of additional 'viability / capacity to pay' tools would impose additional costs and red tape on the taxpayer, their intermediaries and the ATO, without necessarily delivering a commensurate increase in the number of sustainable payment arrangements. This would also inhibit the ATO's ability to increase taxpayer self-management (for example, payment arrangements) through digital channels, which is widely sought by taxpayers and intermediaries with short term cash flow issues.

ATO DEBT RELEASE FOR SERIOUS FINANCIAL HARDSHIP

- 3.40 Stakeholders have observed that the ATO rarely releases taxpayers from debts on the basis of serious financial hardship. The concern is that the requirements are set too high such that debt release is effectively non-existent.

ATO materials

- 3.41 The Commissioner has the discretion to release an individual taxpayer (or the trustee of a deceased estate of an individual taxpayer) from certain tax liabilities, interest and penalties in cases of serious hardship.³⁰⁶ As the powers are discretionary, the Commissioner may refuse debt release even where serious hardship would result from the payment of the tax liability.³⁰⁷ When release is granted, however, the amounts are expunged and may not be re-raised at a later date.

³⁰⁶ Taxation Administration Act 1953 sch 1 ss 340-5, 340-10.

³⁰⁷ *Rollo v Morro* (1992) 23 ATR 447; *Corlette v. Mackenzie* 96 ATC 4502; (1996) 32 ATR 667.

- 3.42 The term ‘serious hardship’ is not defined at law and takes its ordinary meaning. The ATO’s Practice Statement PS 2011/17 describes that it considers serious hardship to occur where the consequences of paying the tax would be so burdensome that the person would be deprived of necessities according to community standards, such as food, clothing, medical supplies, accommodation and education for children.³⁰⁸
- 3.43 The above practice statement also describes that the ATO determines the existence of hardship based on income/outgoing tests, asset/liabilities tests as well as other factors.
- 3.44 The income/outgoing tests aim to quantify the taxpayer’s capacity to meet the tax liability from their current income within a reasonable timeframe. Where a taxpayer incurs above-average expenditures, such as on food, clothing, travel, entertainment or motor vehicles, this would usually lead the ATO to conclude that capacity to pay exists if such expenditures are considered discretionary.³⁰⁹
- 3.45 The assets/liabilities tests aim to determine whether a taxpayer’s equity indicates capacity to pay the tax debt as well as whether acquisition of assets have been unreasonably prioritised ahead of meeting tax liabilities. Subject to the following assets being modest, the ATO would not expect a taxpayer’s residence, furnishings or motor vehicle to be sold to meet tax debts. Other assets may be expected to be realised to meet tax debts.³¹⁰
- 3.46 The other factors which may be considered, include whether a taxpayer has made provision for future tax debts such as disposing of assets without providing for the tax liability, other creditors such that hardship would not be avoided or paying those creditors in preference to the ATO, short term financial difficulties or poor compliance history.³¹¹
- 3.47 Based on the above considerations, the ATO may either not grant release or grant partial or full release. Taxpayers who are dissatisfied with the decision may lodge an objection under Part IVC of the TAA 1953, seek review by the Administrative Appeals Tribunal (AAT) or appeal to the Federal Court.³¹²
- 3.48 An ATO debt hardship team processes all release applications. Any decision by the debt hardship team to release amounts greater than \$5,000, grant partial release or refuse release requires two officers to support that decision.³¹³ There is also a complex case team who may be referred more difficult cases for their review and decision, such as those involving multiple associated entities.³¹⁴

308 ATO, *Debt Relief*, PS LA 2011/17, 3 July 2014, paras [24]-[25].

309 Ibid, paras [29]-[31], ATO, ‘Debt Business Line: Hardship Referral Fact Sheet’ (Internal ATO document, 2011).

310 ATO, ‘Debt Relief’, above n 308, paras [32]-[36].

311 Ibid, paras [37]-[38].

312 Ibid, paras [39]-[40].

313 ATO, Communication to the IGT, 18 November 2014; ATO, Communication to the IGT, 12 December 2014; ATO, ‘Release - Prepare a Recommendation’ (Internal ATO document, March 2014).

314 ATO, Communication to the IGT, 1 April 2015.

- 3.49 The table below outlines the relevant authorisations for which officers can grant release. It is noted that these authorisations were modified during the review.³¹⁵

Table 3.1: ATO staff authorisations to grant release

Officer level	APS1	APS2	APS3	APS4	APS5	APS6	EL1	EL2	SES
Liability	–	–	\$5K	\$20K	\$50K	\$100K	\$250K	∞	∞

Source: ATO, 'Taxation authorisations guidelines' (Internal ATO document, November 2014).

- 3.50 The table below outlines the extent to which the ATO has granted debt release over a three-year period.

Table 3.2: Value of release granted over 2011–12 to 2013–14

	2011–12		2012–13		2013–14	
	No. cases	Value	No. cases	Value	No. cases	Value
Applications received	6,165	\$238,731,342.60	8,878	\$347,674,842.63	9,742	\$384,855,099.69
Full release	2,399	\$57,577,796.46	2,462	\$58,189,177.04	2,266	\$48,736,444.59
Partial release	40	\$3,052,482.41	63	\$3,586,952.33	76	\$3,896,072.17
Refused	1,424	\$138,288,660.90	2,723	\$101,392,317.10	3,658	\$149,079,093.11
Not yet decided*	1,573	\$19,471,622.06	3,289	\$24,926,084.12	3,968	\$13,546,245.10

Note 1: applications received value is not reconciled and includes both eligible and ineligible amounts.

Note 2: refused values have not been reconciled and only includes eligible debt.

Note 3: statics provided represent 'stock on hand'.

Source: ATO.

- 3.51 That ATO has also advised that between 2011–12 and 2013–14, six objections have been allowed in part with all others either invalid, withdrawn or disallowed. Furthermore, all decisions reviewed by the AAT have been upheld in the ATO's favour.³¹⁶
- 3.52 The ATO also periodically engages an external consultant to review a sample of debt release cases. Over the period 2012 to 2014, the consultant found that the majority of cases were in accordance with the ATO's policies. In three sample cases over this period, the consultant found that the hardship tests were not applied correctly.³¹⁷

IGT observations

- 3.53 Releasing individual taxpayers who would otherwise face serious financial hardship from some or all of their liabilities provides them with some financial relief. Such relief potentially reduces the level of support that may be sought from other government sources, such as Centrelink. It is also important that a level playing field is maintained amongst all taxpayers including those who are meeting their obligations and that assistance is not provided to those who are deliberately attempting to avoid their liabilities.

³¹⁵ ATO, 'Process Improvements 2013/14' (Internal ATO document, undated).

³¹⁶ ATO, Communication to the IGT, 3 March 2015.

³¹⁷ PWC, 2012 Release Review: Overarching Report (2012); PWC, 2013 Release Review: Overarching Report (2013); PWC, 2014 Release Review: Overarching Report (2014).

- 3.54 Any decision, as to whether an individual taxpayer may suffer serious financial hardship, is discretionary and release may not be provided even where hardship would be suffered. However, the ATO recognises that such decisions should not be arbitrary³¹⁸ and refusal will be based on the three tests described in the section above. These tests attempt to provide a 'practical structure ... to ascertain whether a person would suffer'³¹⁹ 'serious hardship' as the term is not defined in the law.
- 3.55 In determining serious hardship, it is important to recognise economic impacts on taxpayers' finances, such as increased costs of living over time. Similarly, movements in social norms may also need to be analysed, for example, what may be considered 'serious hardship' now, may not have been in the past due to a range of factors. This is a complicated analysis for the ATO to take into account in making release decisions. Accordingly, it would be beneficial if the ATO consulted with relevant government agencies or conducted research to gain a better insight as to what may be considered 'serious hardship' in today's environment. The ATO uses such an approach when determining individuals' capacity to pay using the DST which is based on the 'Henderson poverty line' described in Chapter 1. The DST could also be used to analyse serious financial hardship.
- 3.56 As set out in the previous section, the other factors considered by the ATO as part of its third test are considerably wider than those considered in the first two tests and may lead to denial of release applications even where serious hardship would occur. Accordingly, it would be beneficial to have more guidance about the circumstances that may be considered. For example, in *Watson and Commissioner of Taxation*,³²⁰ despite the applicant being 61 years of age, having medical illness and with young dependent children, it was found that release was inappropriate despite the payment of tax liabilities resulting in serious financial hardship. This was because, amongst other reasons, the taxpayer's position was largely of their own making as the applicant earned significant income when the liabilities arose but elected not to pay them. The IGT believes that, whilst guidance should be principle-based, better guidance for taxpayers around the factors and how they are weighed would provide them with greater clarity with what to expect in relation to the ATO's debt release decisions.
- 3.57 The IGT also observes that the ATO's application form does not refer taxpayers to PS LA 2011/17 and does not describe the decision stages or the factors that will be considered by the ATO in making a decision. If such reference was made, taxpayers and their advisers may be better aware of the types of information that could be provided to enable the ATO to make informed decisions without the need to request additional information. It would also engender more public confidence in this aspect of tax administration.

318 ATO, 'Debt Relief', above n 308, paras [38].

319 *Rasmussen v Commissioner of Taxation* 2013 ATC 10-337.

320 [2014] AATA 823.

- 3.58 The IGT believes that if the application form for release incorporated the above information it may also assist to reduce the number of applications made for amounts that are ineligible for release, particularly as the ATO statistics suggest a large proportion of release applications may have been refused for this reason (up to 45 per cent).³²¹
- 3.59 The underlying objective of debt release may also be effected by other means, albeit not to the extent of extinguishing the legal liability to pay. For example, where the ATO processes treat a debt as uneconomical to pursue, recovery actions may be stayed until such time that the taxpayer has capacity to pay or has generated a tax credit. Such assistance was provided in *Watson and Commissioner of Taxation*³²² mentioned above. The IGT acknowledges that such a process is described in the ATO's practice statement. However, the day-to-day operational Script Manager and Reference Tool (SMART) system did not discuss this type of assistance. Towards the end of this review, the ATO advised the IGT that it has now updated the SMART system to provide the appropriate guidance.

RECOMMENDATION 3.2

The IGT recommends the ATO:

- (a) consult with relevant government agencies to more appropriately identify the contemporary nature of 'serious hardship' and to use appropriate tools in identifying individual cases;*
- (b) review its guidance and publications to make the circumstances clearer as to where a release is likely to be granted and where it may not be granted for 'serious hardship' cases (including system procedures for staff decisions, such as alternatives to release).*

ATO response: Agree

The ATO has commenced consultation with key financial institutions and government agencies to identify factors taken into account in assessing hardship.

We continuously review and improve our processes, including those relating to release. We are currently reviewing our broader web and other material to ensure information is easy to find and understand.

³²¹ These statistics have not been reconciled by the ATO.

³²² [2014] AATA 823.

ATO REMISSION OF INTEREST

- 3.60 Stakeholders have observed that interest, accumulating to amounts which are disproportionate to the underlying tax debt, may be a disincentive for taxpayers to pay. They have also observed that it has become more difficult to have interest remitted since the GFC. However, stakeholders believe that the ATO could better encourage payment by remitting interest, for example, when offering payment arrangements. The ATO could also better encourage earlier payment by stating on its payment reminders that partial remission may be considered where payment is received within a certain timeframe.
- 3.61 Furthermore, some stakeholders believe that tax agents should be able to remit low risk interest amounts via the Tax Agent Portal to help bring non-lodging taxpayers back into the system. Such an arrangement will be discussed in Chapter 5 in the context of the ATO's use of EDCAs.
- 3.62 Stakeholders have also observed that the ATO imposes conditions on the remission of interest which they believe is inappropriate, such as remission being contingent on future economic performance which may be outside of the taxpayer's control.
- 3.63 Furthermore, stakeholders contend that where the ATO does remit interest, it does so inconsistently. For example, in one case, an amount of approximately \$23 in interest was outstanding which stakeholders believe would ordinarily be remitted as a matter of course. However, only after the ATO had issued a letter demanding payment, the amount was subsequently remitted.
- 3.64 Concerns were also raised in relation to the ATO's remission of penalties which can form part of a taxpayer's total debt. The IGT has considered concerns in relation to penalties in his *Review into the Australian Taxation Office's administration of penalties*.³²³

ATO materials

- 3.65 Legislation imposes GIC which is designed to encourage timely payment of tax as well as compensating the government for late payments. It also removes the advantage that late payers would have over those who pay on time.³²⁴
- 3.66 The rate of GIC (post July 2001) is the monthly average yield of 90 day bank accepted bills for a prescribed month, published by the Reserve Bank of Australia, plus an uplift factor of 7 percentage points which compounds on a daily basis. The uplift factor is intended to dissuade taxpayers from using tax debts as a source of finance. It should be noted that the payment of GIC is a deduction in the year in which it is incurred and conversely interest remitted is assessable income.³²⁵

³²³ IGT, 'Penalties review', above n 120, pp 12-15, 34-35, 40-41, 58, 78, 88-92.

³²⁴ ATO, *Administration of General Interest Charge (GIC) Imposed for Late Payment or Under Estimation of Liability*, PS LA 2011/12, 19 December 2013, paras [25]-[26].

³²⁵ Ibid, paras [4], [12]-[15].

- 3.67 Section 8AAG of the TAA 1953 provides the Commissioner with discretion to remit interest in relation to late payments where the ATO is satisfied that either of the following apply:
- where the delay in payment was caused by circumstances not attributable to the taxpayer and the taxpayer had taken reasonable action to mitigate those circumstances;
 - where the delay in payment was caused by circumstances attributable to the taxpayer and the taxpayer had taken reasonable action to mitigate those circumstances, it would be fair and reasonable to remit all or part of the interest having regard to the nature of the circumstances; or
 - there are special circumstances because of which it would be fair and reasonable to remit all or a part of the charge or it is otherwise appropriate to do so.
- 3.68 Whether remission is to be granted also depends on the risk the ATO attributes to the case, for example, smaller amounts and where the taxpayer has a good compliance history are generally remitted.³²⁶ Partial remission may be considered where taxpayers would not qualify for full remission, for example, in a case where taxpayers were not always compliant or where the taxpayers contributed to the circumstances which resulted in late payment.³²⁷
- 3.69 Circumstances, where the ATO does not attribute the cause of the late payment to the taxpayer, include natural disasters, industrial action, unforeseen collapse of a major debtor or the sudden ill health of the taxpayer. Remission may also be considered where a taxpayer demonstrates that plans were in place to ensure the payment of tax on time, but that as a result of the unforeseen circumstances, payment on time was not possible. General statements such as adverse business conditions affecting an industry or general economic downturn are not acceptable.³²⁸
- 3.70 Where payment delays are attributable to the taxpayer, the ATO will take into account the following factors:
- the intention of GIC to encourage timely payment, discourage the use of tax as finance and compensate the government for the delay in payment; and
 - remission must be fair to the taxpayer having regard to the nature of specific events and also fair to the community, for example, the taxpayer should not be given any advantage over others who pay on time.³²⁹
- 3.71 Accordingly, the ATO will consider whether it is fair and reasonable to remit interest from the perspective of ordinary reasonable community members who pay their taxes on time. For example, whether partial or full remission of interest would avoid serious hardship.³³⁰

³²⁶ ATO, 'Debt Risk Management', above n 237, para [5]; ATO, 'Debt - Low Value Activity Guidelines' (Internal ATO document, October 2014).

³²⁷ ATO, 'Administration of GIC' above n 324, para [34].

³²⁸ Ibid, paras [35], [36], [39].

³²⁹ Ibid, para [43].

³³⁰ Ibid, paras [44]-[46].

- 3.72 The 'otherwise appropriate' discretion gives the ATO flexibility in relation to remitting interest, such as responding to changing circumstances, considering unusual factors or future issues. Such considerations may be in relation to a particular taxpayer but in practice it is more likely to concern a particular group of taxpayers, such as the ATO's 2004 small business initiative whereby such businesses with debts under \$25,000 could enter into extended payment arrangements and could also be eligible for full or partial remission of interest for the period of payment depending on their particular circumstances.³³¹
- 3.73 Practice Statement PS LA 2011/12 also describes specific situations where it may be fair and reasonable to remit interest. For example, where a taxpayer has entered into a 50/50 arrangement in relation to disputed debts, where litigation is funded under the ATO's test case litigation program and in insolvency where all other creditors agree to forgo their claims to interest.³³²
- 3.74 Generally, a taxpayer must request remission of interest and demonstrate that remission is warranted. However, where the circumstances which justify remission are readily apparent, the ATO may initiate remission.³³³ The ATO has also advised that the decision to remit GIC is based on circumstances at the time of the decision and is not subject to a later reversal of that decision. Overall, the Commissioner does not impose conditions when remitting or considering remission of GIC.³³⁴
- 3.75 The ATO has also advised that there are automated processes which remit GIC on some amounts which are below the remission threshold. For manual processes, the ATO limits the amounts DBL officers are authorised to remit which are outlined in the table below.³³⁵

Table 3.3: ATO staff authorisations for remitting interest

Officer level	APS1	APS2	APS3	APS4	APS5	APS6	EL1	EL2	SES
General remission									
Max. amount	\$5K	\$10K	\$25K	\$75K	\$100K	\$250K	∞	∞	∞
Remission otherwise appropriate									
Max. amount	–	–	–	–	–	–	–	Yes	Yes
Remission otherwise appropriate: small business initiative									
Max. amount	–	–	Yes	Yes	Yes	Yes	Yes	Yes	Yes

Source: ATO, 'Tax authorisation guidelines' (Internal ATO document, November 2014).

331 Ibid, paras [51]-[53], [55].

332 Ibid, paras [51]-[53], [55].

333 Ibid, para [28].

334 ATO, Communication to the IGT, 5 March 2015.

335 ATO, Communication to the IGT, 12 December 2014.

IGT observations

- 3.76 As mentioned earlier, there may be situations where taxpayers, despite their best intentions, enter into unaffordable payment arrangements. In such circumstances, GIC may have escalated to an extent where the debt becomes unmanageable. Remission of GIC in part or whole, in such cases, may have been enough to maintain their previous willingness to engage with the ATO. For example, the IGT agrees with stakeholders that the ATO could better encourage earlier payment by stating on its payment reminders that partial remission may be considered where payment is received within a certain timeframe.
- 3.77 As mentioned in Chapter 2, the ATO has recognised that there may be a ‘tipping point’ for the effectiveness of the GIC and is currently conducting research and is analysing the ‘next best action’ approach to encourage particular taxpayers to pay their debts including by remitting interest. The outcomes of this work could be used to identify factors which result in timely payment when interest is remitted as opposed to allowing a debt to continue with GIC accruing. Such an approach could also minimise the extent of serious financial hardship or insolvency.
- 3.78 The IGT observes that the ATO’s materials are silent as to whether, firstly, it can impose conditions on interest remission and, secondly, whether it can overturn remission decisions where those conditions are not satisfied. However, the ATO has advised that it does impose conditions on remission of GIC. Accordingly, the issue may more likely be attributable to the need for better supervision of ATO officer decisions which will be discussed in Chapter 4.

RECOMMENDATION 3.3

The IGT recommends the ATO:

- (a) *engage with taxpayers in discussions on remission of interest as a means of supporting prompt payment of debt by, for example, including on payment reminders that partial remission may be granted where debts are paid promptly; and*
- (b) *based on the findings of its research into ‘tipping points’ and the ‘next best action’ consider remitting interest in appropriate cases to further encourage prompt payment.*

ATO response: Matter for Government

CHAPTER 4 – ATO FIRMER DEBT RECOVERY ACTIVITIES

- 4.1 Following the GFC, the amount of debt owed to revenue authorities has increased. In response, many revenue authorities have sought to utilise a range of treatments, including firmer debt recovery activities, to improve tax collection.³³⁶
- 4.2 In Australia, generally, where taxpayers do not pay their liabilities on time and the ATO determines that there is a risk of non-payment, the ATO may seek to recover the debt through a range of firmer recovery options as listed in Chapter 1.

SUMMARY OF STAKEHOLDER CONCERNS

- 4.3 Many stakeholders have raised a range of concerns with a number of the ATO's firmer debt recovery activities. These concerns may be distilled into three main themes:
- inadequate supervision of staff to ensure ATO officers chose the recovery mechanism that is most appropriate to taxpayers' circumstances and that cases are effectively managed;
 - inappropriate ATO staff conduct, such as infrequent and aggressive communications; and
 - inaccurate information which resulted in unnecessary recovery activities, such as where amounts have been paid or no notification was received by taxpayers before firmer action commenced.
- 4.4 The above themes will first be addressed through an analysis of each firmer recovery activity specifically raised by stakeholders.
- 4.5 Following the discussion on the specific firmer debt recovery activities, the broader themes will then be discussed.

SPECIFIC DEBT RECOVERY ACTIVITIES

Garnishee notices

- 4.6 Stakeholders have observed that the ATO had sometimes issued garnishee notices:
- where no debt existed such as where the Tax Agent Portal showed that tax had been paid as well as where PAYG Instalments had been correctly varied;
 - with incorrect details such as wrong bank account or legal entity;

³³⁶ OECD, 'Tax Debt Management', above n 45, p 18.

- in inappropriate situations such as where taxpayers were unaware of audit finalisation and where the notice was actioned by third parties before taxpayers were notified;
- for significant and disproportionate amounts without consideration of taxpayers' circumstances or future viability which forces taxpayers towards unnecessary insolvency, for example, by garnishing the majority funds within bank accounts; and
- which were not revoked or refunded in appropriate situations such as where matters have been decided in the taxpayer's favour or where the taxpayer was in the process of settling a disputed liability in their favour.

ATO materials

- 4.7 The ATO has advised that its accounting and registration systems, being the Integrated Core Processing (ICP) and ATO Integrated System (AIS), contain the data upon which it relies for commencing debt recovery action.³³⁷ These systems are designed to account for debits, credits and due dates pursuant to legislative requirements.³³⁸
- 4.8 Furthermore, there are processes which align the information contained in ICP and AIS with the ATO's case management systems, Siebel and the Receivables Management System (RMS) respectively. Siebel is used to manage income tax cases whereas RMS is used to manage other amounts, such as activity statement and superannuation guarantee amounts. Updates to the case management systems occur overnight. Should a mismatch between ICP and Siebel occur, the case is held until consistency is achieved.³³⁹ For AIS and RMS, the ATO has advised that staff may manually check AIS directly and use a 'refresh' button in RMS to update information.³⁴⁰
- 4.9 The ATO has also advised that it builds delays into its debt recovery processes in both RMS and Siebel to allow case information to be updated before proceeding with recovery actions.³⁴¹ The ATO has advised that some payment processing times cannot be addressed due to different payment channels and the various intermediaries involved.³⁴² Appendix 9 contains the ATO processing times for the different payment channels.
- 4.10 Where a debt is shown to exist in the ATO systems, the ATO will consider whether to issue a garnishee notice. These considerations were described in Chapter 1.

³³⁷ ATO, Communication to the IGT, 29 October 2014.

³³⁸ Ibid.

³³⁹ Ibid.

³⁴⁰ ATO, Communication to the IGT, 1 April 2015.

³⁴¹ ATO, Communication to the IGT, 29 October 2014.

³⁴² ATO, Communication to the IGT, 6 March 2015.

- 4.11 Before issuing a garnishee notice, however, ATO staff are directed to check all accounts of the taxpayer for any payments received or credits applied as the ATO would have sent a warning letter to the taxpayer by this stage. As part of this process, staff are required to ensure that payments and credits have been applied to the correct taxpayer account. Furthermore, staff are required to identify whether payments have been made pursuant to a payment arrangement.³⁴³
- 4.12 ATO staff are then required to identify appropriate financial accounts by using the ATO's Compliance Online Enquiry and Amendment System which, amongst other things, matches Tax File Numbers (TFN) with bank accounts. In this respect, as mentioned in Chapter 1, staff are directed not to issue garnishee notices in relation to bank accounts which are in joint names, do not match the taxpayer name or certain account types (for example, funds held on trust).³⁴⁴ In other procedures, staff are expected to revoke garnishee notices where they have been incorrectly issued such as where the funds are not the property of the taxpayer (such as being held in a trustee) or obtained as a result of a bank error.³⁴⁵
- 4.13 The ATO has also identified in an internal complaints report, a case which resulted in the garnishing of an account unrelated to a taxpayer. The ATO determined that this issue was either due to 'an ATO error in data matching [systems], an error by the ATO officer issuing the garnishee and possibly a lack of information in SMART'. The report contended, however, that the particular bank was also at fault as banks are required to identify the correct accounts to garnishee.³⁴⁶
- 4.14 The ATO has also found in another internal report on the quality of garnishee notices that 38 per cent of sampled cases did not meet procedural requirements. In these cases, staff were not issuing copies of the 'point in time' garnishee notices to the relevant parties as outlined in the ATO's procedures in the SMART system – staff were missing the requirement to identify the parties required to be issued with a copy of the garnishee notice based on the entity type.³⁴⁷
- 4.15 In addition to the considerations described in Chapter 1, the ATO's procedures also direct ATO staff to review the case history, file notes, audit reports as well as consider contacting the previous case officer (for example, auditor or objection officer) to discuss their findings to verify the decision to issue a garnishee notice.³⁴⁸ If staff are unsure about the next course of action, or if any instructions are unclear, they must consult coaching staff or their team leader.³⁴⁹

343 ATO, 'PIT garnishee notice', above n 59.

344 Ibid.

345 ATO, 'Debt Reference Manual', above n 66, [Garnishee notices].

346 ATO, 'Garnishees Issued and Complaints Received 2014 – 15' (Internal ATO document, undated).

347 ATO, 'Debt Business Line - Garnishee Review - Final Report' (Internal ATO document, August 2013) p 3.

348 ATO, 'PIT garnishee notice', above n 59; ATO, 'Significant Debt Management', above n 63, p 16.

349 ATO, 'PIT garnishee notice', above n 59.

- 4.16 Taxpayers must also generally be warned of a potential garnishee notice.³⁵⁰ In this respect, staff are required to search the AIS for valid taxpayer addresses, including checking for 'incorrect return indicators'. Where such indicators are present, staff are required to search for suitable alternatives, such as for any associated tax agents. Where suitable addresses cannot be found, garnishee notices are not expected to be issued.³⁵¹
- 4.17 The ATO, however, has also found as part of an internal review that some FAW letters were sent to outdated addresses. The report of the review notes, in accordance with ATO procedures, that FAW letters are sent to 'postal addresses' whereas garnishee notices are sent to 'residential addresses' in ATO systems. As a result of the different addresses used, the report noted that there is a need to review relevant processes.³⁵²
- 4.18 When issuing a garnishee notice, staff are also required to consider the amount or proportion and financial impact on taxpayers as mentioned in Chapter 1.³⁵³ Furthermore junior ATO staff at the Australian Public Service (APS) 2 level are authorised to issue garnishee notices for amounts up to \$50,000 with progressive authorisations until the APS 5 level staff who have no limit on the amount for which they can issue garnishee notices.³⁵⁴
- 4.19 Statistics provided by the ATO, reproduced in Table 4.1 below, show the number of cases where garnishee notices issued and those cases where the taxpayer subsequently became insolvent.

Table 4.1: Solvency following the use of garnishee notices

Business segment	2011–12 (number of cases)	2012–13 (number of cases)	2013–14 (number of cases)	Total (number of cases)	Percentage
GOV	4	1	1	6	0.00%
Insolvent	0	0	0	0	0.00%
Solvent	4	1	1	6	100.00%
INB	6,485	13,878	8,965	29,328	14.15%
Insolvent	0	3	0	3	0.01%
Solvent	6,485	13,875	8,965	29,325	14.15%
LGE	25	41	59	125	0.06%
Insolvent	0	0	0	0	0.00%
Solvent	25	41	59	125	100.00%
MIC	37,198	65,281	58,222	160,701	77.55%
Insolvent	0	346	283	629	0.39%
Solvent	37,194	64,920	57,938	160,052	99.60%
Unknown	4	15	1	20	0.01%

350 ATO, 'Debt Reference Manual', above n 66, [Garnishee notices].

351 ATO, 'PIT garnishee notice', above n 59.

352 ATO, 'Garnishees and Complaints', above n 346.

353 ATO, 'Enforcement Measures', above n 56, para [102].

354 ATO, 'Taxation Authorisation Guidelines', above n 75, para [1.14].

Table 4.1 (continued)

Business segment	2011–12 (number of cases)	2012–13 (number of cases)	2013–14 (number of cases)	Total (number of cases)	Percentage
NFP	132	151	85	368	0.18%
Insolvent	0	1	2	3	0.82%
Solvent	132	150	83	365	99.18%
SME	5,024	5,979	5,692	16,695	8.06%
Insolvent	0	79	67	146	0.87%
Solvent	5,024	5,893	5,621	16,538	99.06%
Unknown	0	7	4	11	0.01%
Grand Total	48,868	85,331	73,024	207,223	100.00%

Source: ATO Communication to the IGT, 9 October 2014.

- 4.20 The table above shows that the majority of garnishee notices are issued to individual and small business taxpayers. Furthermore, a small proportion of all taxpayers subsequently became insolvent following the issuing of a garnishee notice based on the data provided.
- 4.21 Chapter 1 noted that both the EI and SDM units can issue garnishee notices and deal with low and high risk cases respectively. In doing so, they take a different approach to managing cases. In low risk cases, a summary of all interactions and decisions are recorded against the taxpayer's account and is referred to by subsequent ATO staff when interacting with the taxpayer and/or taking actions to collect the outstanding debt.³⁵⁵ For high risk cases, the SDM unit will assign a single case officer to manage a case.³⁵⁶
- 4.22 With respect to case management, the earlier mentioned ATO quality report, found that 15 per cent and 63 per cent of cases met the standards in relation to updating systems and quality notes respectively. For example, staff were not using appropriate systems' codes (for example, RMS, Siebel or finalisation codes) to update the relevant system when completing cases as well as not including all relevant information in their case narratives when actioning garnishee notices.³⁵⁷
- 4.23 The quality report also found that the majority of cases which did not meet standards were those conducted by the former Early Collections unit (75 per cent of sampled cases) and Firmer Action unit (25 per cent of sampled cases).³⁵⁸
- 4.24 In an ancillary assessment, the quality report reviewed the appropriateness of situations, including where:
- 1) payment arrangements were entered into after the issuing of a 'point in time' garnishee notice; and

³⁵⁵ ATO, Communication to the IGT, 21 January 2015.

³⁵⁶ Ibid.

³⁵⁷ ATO, 'Garnishee Review', above n 347, p 3.

³⁵⁸ Ibid, p 2.

- 2) garnishee notices (both standard and point in time) issued on accounts where there have been payments made in response to the issue of a warning letter.³⁵⁹
- 4.25 In the first situation, the ATO found that in 28 per cent of the sampled cases, staff did not take into consideration the issuing of the garnishee notice when negotiating the payment arrangement.
- 4.26 In the second situation, in 48 per cent of sampled cases, the issuing of the garnishee notice was found to be inappropriate for the following reasons:
- regular payments had been made to the account prior to and post issue of the FAW letter and no further or insufficient phone contact had been attempted before issuing of the garnishee notice;
 - no consideration was given to the taxpayer's circumstances including whether financial hardship existed or an expected income tax refund was due which would have cleared the outstanding debt;
 - the only attempt at contact with the taxpayer prior to the issue of the garnishee notice was in the issue of the FAW letter;
 - the garnishee notice was issued following a defaulted payment arrangement and further payment arrangements were not entered, however, consideration was not given to the reasons for the default, for example, due to the imposition of FTL penalties which were subsequently remitted;
 - phone contact directly with the taxpayer, rather than their tax agent, may have been more appropriate prior to the issue of a garnishee notice as all attempts to contact the tax agent had been unsuccessful; and
 - the case notes did not support the decision to issue.³⁶⁰
- 4.27 The ancillary assessment in the quality report also found a number of procedural inconsistencies with respect to garnishee notices, including:
- Early Collections unit procedures for 'point in time' garnishee notices do not prompt staff to check if the taxpayer is a low income earner prior to determining whether the issue of the notice is appropriate whereas the procedures for the former Firmer Action unit did do this, including prompting them to consult with their team leader or coach to determine whether the issuing of a garnishee notice is appropriate given the taxpayer's circumstances; and
 - lack of staff guidance with respect to determining whether a taxpayer is a lower income earner based on their most recent tax return (within the last two years) where their last lodged return is more than two years old.³⁶¹

359 Ibid, p 5.

360 Ibid, p 6.

361 Ibid.

- 4.28 Towards the end of this review, the ATO management made representations to the IGT that the quality reports were commissioned to review the work of casual staff engaged by the ATO at the time. As a result of the review, the issuing of garnishee notices was suspended until staff received further training. Furthermore, the ATO considers that a number of structural and staffing changes have occurred since the quality reviews.³⁶² The ATO's management have also represented that the inconsistencies in the procedures have since been recently corrected.³⁶³
- 4.29 The ATO has also advised that a more recent quality review of 22 cases, based on an updated process which is described later in this Chapter, identified one case where standards were not achieved.³⁶⁴

IGT observations

- 4.30 Garnishee notices are the most common form of firmer recovery action used by the ATO, with over 207,000 notices issuing between 2011–12 and 2013–14. Accordingly, it is vital that garnishee notices are issued correctly as they impact a significant number of taxpayers every year.
- 4.31 Accordingly, there are a range of improvements which the ATO could make to its systems and staff procedures to help ensure garnishee notices are issued correctly.
- 4.32 The IGT acknowledges that the ATO has attempted to design its payment and case management systems to ensure that firmer recovery action is based on accurate information and appropriate procedures. However, based on the information the ATO provided, adequate processes are not in place to correct cases where there is a mismatch between data contained in AIS and RMS systems specifically. This appears to align with stakeholder concerns which indicate that garnishee notices have mostly issued incorrectly for amounts recorded on these systems. Clearly, improvements are required to eliminate the possibility of staff basing their decisions on inaccurate information.
- 4.33 Furthermore, ATO quality reports have identified that staff may not be following procedures which require them to check the accuracy of systems data before issuing garnishee notices. The ATO, however, believes that there are no systemic issues with respect to the accuracy of information on which garnishee notices are issued despite difficulties identifying whether any corrective action was needed. The ATO also believes that such complaints represent a small proportion of total garnishee notices issued and that its new quality system has not identified any significant issues in a sample of 22 cases.³⁶⁵ However, the sample size is relatively small given that the ATO has issued over 200,000 garnishee notices over a three-year period. Given the significant potential impact on taxpayers, there is a need to better supervise staff to ensure that they are making the required checks. The need for better supervision is further discussed later in this chapter.

³⁶² ATO, Communication to the IGT, 1 April 2015.

³⁶³ Ibid.

³⁶⁴ Ibid.

³⁶⁵ ATO, Communication to the IGT, 9 March 2015.

- 4.34 The IGT also acknowledges that the ATO has procedures which require staff to ensure that garnishee notices are issued with respect to the correct bank account. However, it appears that the procedures rely on taxpayers to raise concerns that garnishee notices should be revoked, for example, where the funds are held on trust for the benefit of others. Indeed, in this respect, the ATO has found that there may be a lack of information in its SMART system and has updated its procedures accordingly.
- 4.35 Furthermore, the IGT believes that the ATO could more clearly invite challenges from financial institutions where they believe that proposed funds to be garnished do not solely belong to the taxpayer in question. For example, as part of the ATO request to financial institutions, it could also ask whether the account may not be appropriate in relation to the party identified in the garnishee notice.
- 4.36 The ATO has also identified that lower risk taxpayers may not have been warned of the impending garnishee notice. In these cases, the IGT notes that much of the ATO's early contact is through automated mailing processes. Whilst these are highly efficient mechanisms to communicate with the majority of taxpayers, there is less certainty that taxpayers will be contacted. It appears that in these cases, only where firmer action has commenced, will an ATO officer seek to determine appropriate contact details. This may explain why taxpayers receive garnishee notices, for example, but not the earlier warning. Clearly, if the ATO has a policy of warning lower risk taxpayers, it should ensure adherence to this policy. To this end, the IGT believes that the ATO should ensure its officers make every effort to contact the taxpayer.
- 4.37 The IGT also observes that junior staff at the APS 2 level are authorised to issue garnishee notices for significant amounts (up to \$50,000). Given the significant amounts which junior officers may issue garnishee notices, the IGT believes that greater supervision of these officers' decisions is required including the need to seek approval from more senior officers before any notices are issued. This will be further discussed later in this chapter.
- 4.38 Lastly, the IGT recognises that the ATO has procedures which require staff to review case history, audit reports and consider contacting the auditor or objection officer to understand the case before issuing a garnishee notice. However, the ATO's internal reports found that a significant number of cases did not adequately update systems or take quality notes in relation to garnishee notices. This may adversely impact the quality of decisions made by officers considering garnishee notices for lower risk cases. Once again, there is a need to ensure that staff follow procedures.
- 4.39 For higher risk cases such as where there are disputed debts, whilst the debt may be managed by a dedicated officer from the DBL, officers from the ATO's legal area may also be involved. In these cases, the ATO has a joint case callover process to promote a consistent approach by both officers. However, in lower risk cases which do not have a similar callover process, there is a risk of inconsistent approaches being taken where there is a lack of communication between the officers. Accordingly, the IGT believes that the ATO should aim to take a unified approach to ensure the decision to issue garnishee notices is appropriate.

RECOMMENDATION 4.1

The IGT recommends that the ATO improve the process for issuing garnishee notices by:

- (a) developing improved processes to correct data mismatches between the ATO Integrated System and Receivables Management System;*
- (b) encouraging financial institutions to challenge garnishee notices where they believe notices may have been issued to the incorrect bank account;*
- (c) reviewing its officers' adherence to policy of making every effort to telephone taxpayers, particularly lower risk taxpayers; and*
- (d) adopting a unified approach between debt and legal officers when issuing garnishee notices for all cases.*

ATO response: Agree in Part

The ATO agrees with (a), (b) and (c). As part of our continuous improvement framework, we will review and refine our garnishee processes, including the rare occurrence of data mismatches, using our quality assurance processes, system controls, stakeholder feedback loops, and identification of best practice.

The ATO disagrees with (d) as there are existing processes in place to ensure a unified approach where 'legal officers' (Review and Dispute Resolution – RDR) are a stakeholder in debt collection action which may necessitate the issuing of a garnishee notice. Where we have referred a taxpayer to RDR to represent the ATO in court on wind-up or bankruptcy hearings, garnishee action will not be taken as we are petitioning the court to determine the taxpayer's solvency. Legal officers, themselves, do not issue garnishee notices.

Director Penalty Notices

4.40 Stakeholders have observed that the ATO has recently made greater use of DPNs and consider them effective in alerting company directors to attend to their tax obligations. However, they have raised the following concerns:

- the DPN regime should be expanded to GST as the policy basis is analogous to using DPNs to recover PAYG Withholding and superannuation guarantee.
- DPNs have a burdensome impact on business viability, particularly for small businesses and 'silent' directors who are commonly spouses or adult children of the taxpayer who do not understand their obligations and as the current defences to DPN liability³⁶⁶ are limited, the grounds for releasing taxpayers from debts due to serious financial hardship should be expanded to allow a distressed company to restructure their financial affairs.

³⁶⁶ Taxation Administration Act 1953 sch 1 s 269-35.

- DPNs are issued automatically and the ATO has removed safeguards for the non-service of demands³⁶⁷ requiring only notices to be posted but not necessarily received.

ATO materials

- 4.41 The ATO can issue a DPN to company directors which can make them personally liable for unpaid PAYG Withholding and SGC liabilities as was explained in Chapter 1.³⁶⁸
- 4.42 The amount of the director penalty is equivalent to the unpaid amount of the company's PAYG Withholding or SGC liabilities.³⁶⁹ The ATO does not have discretion in relation to the quantum of director liabilities under a DPN as it is incurred automatically. However, where a company is unable to pay these amounts, Practice Statement PS LA 2011/18 indicates that the ATO may consider entering into a payment arrangement with the company.³⁷⁰ Materials in relation to the ATO's consideration of whether to enter into payment arrangements were outlined in Chapter 3.
- 4.43 The impact of DPNs on business viability can be inferred from the rate of insolvency following the issuing of a DPN. The table below outlines the ATO's statistics on this issue.

Table 4.2: insolvency following the issuing of a DPN

Business segment	2011–12 (number of cases)	2012–13 (number of cases)	2013–14 (number of cases)	Total (number of cases)	Percentage of Total	Percentage of Grand Total
INB	0	3	1	4	100.00%	0.01%
Insolvent	0	0	0	0	0.00%	0.00%
Solvent	0	3	1	4	100.00%	0.01%
LGE	13	31	33	77	100.00%	0.28%
Insolvent	13	0	3	16	20.78%	0.06%
Solvent	0	31	30	61	79.22%	0.22%
MIC	5,320	6,277	8,253	19,850	100.00%	71.31%
Insolvent	1,539	1,486	1,572	4,597	23.16%	16.51%
Solvent	3,781	4,791	6,681	15,253	76.84%	54.80%
NFP	87	79	52	218	100.00%	0.78%
Insolvent	3	2	3	8	3.67%	0.03%
Solvent	84	77	49	210	96.33%	0.75%
SME	2,051	2,479	3,156	7,686	100.00%	27.61%
Insolvent	400	393	461	1,254	16.32%	4.50%
Solvent	1,651	2,086	2,695	6,432	83.68%	23.11%

³⁶⁷ *Taxation Administration Act 1953* sch 1 s 269-25(4).

³⁶⁸ ATO, 'Enforcement Measures', above n 56, para [47].

³⁶⁹ *Taxation Administration Act 1953* sch1 s 269-10.

³⁷⁰ ATO, 'Enforcement Measures', above n 56, para [41].

Table 4.2 (continued)

Business segment	2011–12 (number of cases)	2012–13 (number of cases)	2013–14 (number of cases)	Total (number of cases)	Percentage of Total	Percentage of Grand Total
Unknown	1	0	0	1	100.00%	0.00%
Insolvent	0	0	0	0	0.00%	0.00%
Solvent	1	0	0	1	100.00%	0.00%
Grand Total	7,472	8,869	11,495	27,836	—	100.00%

Source: ATO.

- 4.44 The table shows that between 2011–12 and 2013–14, the ATO had issued over 27,000 DPNs primarily to directors of small businesses. Furthermore, approximately 21 per cent of these taxpayers have become insolvent following the issuing of a DPN. Approximately 21 per cent of large businesses have also become insolvent following issuing of a DPN.
- 4.45 The relevant legislation provides for limited defences to DPNs. These may be summarised as follows:
- the director had taken all reasonable steps to either cause the company to comply with its obligations, appoint a company administrator or cause the company to be wound up; or
 - it was unreasonable to expect the director to take part in the management of the company because of, for example, illness.³⁷¹
- 4.46 However, if the obligations were not paid within three months of the due day and the underlying liability remains unpaid and unreported, a director cannot avoid personal liability by appointing a company administrator or wind up the company as mentioned in Chapter 1.³⁷²
- 4.47 It should also be noted that whilst the Commissioner must provide notice to taxpayers of the DPN, such notice is deemed to be given where the Commissioner ‘leaves or posts it’.³⁷³ Further, the ATO is legally required to serve DPNs to directors’ addresses as recorded with ASIC. However, the ATO has a supplementary process to send a photocopy of the DPN to a more recent address for the taxpayer if available.³⁷⁴

371 Ibid, paras [54]–[55]; *Taxation Administration Act 1953* sch 1 s 269–35.

372 *Taxation Administration Act 1953* sch 1 s 269–30(2).

373 *Taxation Administration Act 1953* sch 1 s 269–25(4).

374 ATO, Communication to the IGT, 1 April 2015.

- 4.48 An internal ATO quality report on DPNs found that in 50 per cent DPNs sampled, actions did not meet the ATO's requirements in relation to 'appropriate interaction' (40 cases). In 55 per cent of these cases, this was due to an alternative or more recent address being available and a copy of the DPN was not sent to that address despite staff procedures requiring a photocopy of the DPN to be sent to the alternative address.³⁷⁵ In 38 per cent of these cases, incorrect or inaccurate periods were specified on the DPN, including issuing the wrong DPN variant as well as incorrectly allocating amounts with respect to DPNs.³⁷⁶
- 4.49 Towards the end of the review ATO management made representations that, since the abovementioned review, it had clarified the processes with respect to mailing copies of DPNs to more recent addresses, provided staff training on worksheets used to allocate payments/credits to correct periods and developed a macro which automatically applies the payment/credits allocation rules for staff.³⁷⁷

IGT observations

- 4.50 The DPN regime applies to protect employees by ensuring that amounts withheld from their pay in relation to their tax liability and superannuation can be recovered from company directors where those amounts were not remitted to the ATO. The DPN regime also limits a company director from escaping their liability where the company is put into liquidation.
- 4.51 The Treasury, in its 2009 proposal paper, has raised the idea of the DPN regime being extended to GST liabilities amongst others:

...a limitation of the existing director penalty regime is that it does not extend to all types of liabilities that are often left unpaid as a result of fraudulent phoenix activity.

While extending the director penalty regime to cover liabilities such as [superannuation guarantee and] indirect taxes (for instance GST and excise)... would go beyond the original policy intent behind the regime... there may be justification for doing so. Certainly, in the context of SG amounts, there are arguably strong public interest grounds to increase the incentives for directors to ensure that their company complies with their [superannuation guarantee] obligations as there is a direct impact on the employee if they fail to do so.

While other taxation liabilities, such as indirect taxes (like GST and excise)... do not relate to the liability of another entity, their inclusion in an expanded and amended director penalty regime would nonetheless support its role as a disincentive for directors to engage in fraudulent phoenix activity.³⁷⁸

375 ATO, 'Risk Product Review - Firmer Action Director Penalty Notices (DPN's) Review (Lockdown and Normal) - Final Report' (Internal ATO document, October 2013) p 2.

376 Ibid, pp 2-3.

377 ATO, Communication to the IGT, 1 April 2015.

378 The Treasury, *Actions Against Fraudulent Phoenix Activity* (Proposal, 2009) p 14.

- 4.52 The above idea was not adopted by the then Government. Whilst stakeholders acknowledge the benefit of DPNs to secure superannuation and PAYG Withholding which properly belongs to employees and support its use in this respect, it is uncertain whether the broader public would consider GST to be of the same importance as employee entitlements. Furthermore, if the DPN regime was extended to GST, it would effectively elevate the then Government's standing against employees and other creditors. Such an outcome is contrary to the Government adoption of the recommendations of the 1988 Harmer Report which supported the removal of Commonwealth priority in relation to tax for reasons including:
- the ATO may allow taxation debts to accumulate without prejudicing its position and this may disadvantage other unsecured creditors who may not know that tax is owed;
 - the ATO has no incentive to recover payment in the normal commercial manner;
 - the ATO should obtain no greater priority than any other person claiming in relation to debts misappropriated by the insolvent company; and
 - there would be a reduction in litigation.³⁷⁹
- 4.53 Accordingly, the IGT is of the view that DPNs should not be expanded to GST at the present time.
- 4.54 In relation to stakeholder concerns that DPNs have a burdensome impact on business viability, ATO statistics, presented earlier, show that a substantial proportion of business taxpayers have subsequently become insolvent, following the issuing of DPN notices.
- 4.55 The IGT considers that the significant number of taxpayers that become insolvent following the issuing of a DPN may be due to the defences to personal liability (that is, wind up) or the nature of scenarios in which they are used. These scenarios include not paying employee entitlements which may be due to financial distress rather than malicious intent. Given these considerations and the level of insolvency associated with DPNs, the IGT believes that quick action by the ATO is essential to encourage remedial action by company directors as the viability of a business may quickly deteriorate leaving debts irrecoverable which disadvantages business employees as well as the business itself and its directors.
- 4.56 The critical period is where lodgment/payment was not made and when the ATO subsequently issues a DPN. During this period, the ATO needs to consider interacting with the directors in a 'gentler' way by, for example, also sending directors the lodgment/payment reminders, offers of payment arrangements or promptings to seek professional advice if the business does not appear viable to the ATO. Such actions may prompt directors to take earlier remedial action which would improve the chances of a business avoiding insolvency. Earlier action by the ATO may also lessen the need to use 'lockdown' DPNs or amend legislation to provide taxpayers with additional time to restructure their affairs.

³⁷⁹ Australian Law Reform Commission, *General Insolvency Inquiry Report No 45* (AGPS, 1988) paras [738]-[41].

- 4.57 In relation to reducing the severity of the consequences of DPNs, it may be inappropriate for serious financial hardship to become a defence since the amounts being sought are employee entitlements. Any relief beyond a payment arrangement, such as release, would result in employee entitlements being unpaid. Accordingly, a more appropriate option would be to ensure that directors, particularly those of smaller businesses, are fully apprised of their legal obligations. In this respect, the IGT recommended in Chapter 2 (Recommendation 2.4), that the ATO explore opportunities with other agencies to jointly develop educative materials.
- 4.58 In relation to stakeholder concerns with the deemed service of DPNs, it is an important mechanism for the ATO to protect employee entitlements, such as where directors cannot be located. However, in addition to earlier and less intrusive interactions with directors mentioned above, the ATO should also take all reasonable steps to make contact with directors in connection with issuing DPNs in a similar way as was mentioned in the section on garnishee notices. The IGT considers this issue to be particularly important given that in the quality review, the ATO found that 50 per cent of sampled cases did not follow procedures to ensure DPNs were sent to appropriate addresses. Importantly, directors are not able to take remedial action if they are unaware of the proposed action. In this respect, the IGT recommended in Chapter 2 (Recommendation 2.3(b)), that the ATO ‘take earlier, more frequent and less intrusive debt recovery action to minimise the necessity to take firmer action at a later time’.
- 4.59 Additionally, the quality report also found that incorrect DPN variants have been used, incorrect periods specified, as well as amounts incorrectly allocated. Despite, the ATO management representation made at the end of this review that training and support tools have been created, issues, including those mentioned above, indicate that better supervision is needed, particularly as ATO officers that issue DPNs may be quite junior. Supervision is further discussed in a later section in this chapter.

RECOMMENDATION 4.2

The IGT recommends that, consistent with recommendation 2.3(b), the ATO act sooner and take proportionate actions to prompt company directors to address impending insolvency.

ATO response: Agree

We will take more timely and appropriate action, which will include using our statutory powers where companies have failed to pay amounts withheld from employee's wages or employees superannuation entitlements, to remove any unfair financial advantage taxpayers not doing the right thing might have over those that do comply with their obligations.

Freezing orders

4.60 Stakeholders have cited situations where the use of freezing orders was not considered to be warranted. These examples include:

- whilst the taxpayer was overseas and without knowledge of the outcome of an audit; and
- where a taxpayer was in the process of negotiating a payment arrangement and then was told to borrow money to make an upfront payment.

ATO materials

4.61 The ATO's approach to applying to the court to grant freezing orders was described in Chapter 1.

4.62 As freezing orders involve applications to the court, debt staff are required to refer the matter to the Review and Dispute Resolution (RDR) section of the ATO's Law Design and Practice Group (LD&P). The ATO has advised that the RDR officer will then liaise with the debt officer and make recommendation whether a freezing order should be sought.³⁸⁰

4.63 The courts generally accept that most freezing orders are made ex parte (that is, without taxpayer notice) and restrict the right to deal with assets even before the judgment is handed down. For this reason, the court will require the ATO to make full and frank disclosure of all material facts, including any defences which may support the taxpayer as well as to give undertakings in relation to damages as mentioned in Chapter 1. Furthermore, the court generally only allows freezing orders to be made without notice for one or two days after the order is made. After this time, the taxpayer must have been served with the order and given the opportunity to be heard. The matter then usually returns to court within 7 days. The ATO, however, has the onus to satisfy the court that the order should be continued or renewed.³⁸¹

4.64 In determining whether to proceed with a freezing order, the relevant technical area, the DBL as well as the RDR section should be consulted and such decisions can only be made by Senior Executive Service (SES) officers.³⁸² Between 2011–12 and 2013–14 the ATO had sought a total of 19 freezing orders.³⁸³ The table below outlines by business segment the composition of this total.

380 ATO, Communication to the IGT, 3 March 2015.

381 PA Keane, *Federal Court Practice Note CM 9* (2011); ATO, 'Enforcement Measures', above n 56, paras [179], [193]–[193].

382 ATO, 'Enforcement Measures', above n 56, paras [179], [193]–[193].

383 ATO, Communication to the IGT, 9 October 2014.

Table 4.3: ATO applications for freezing orders by business line

Business segment	2011–12 (number of TFNs)	2012–13 (number of TFNs)	2013–14 (number of TFNs)	Total (number of TFNs)
INB	—	7	—	7
MIC	1	2	1	4
SME	2	1	—	3
Uncategorised	1	1	3	5
Grand Total	4	11	4	19

Source: ATO.

- 4.65 Table 4.3 above shows that of the 19 freezing orders issued by the court on application by the ATO between 2011–12 and 2013–14, 7 were issued to individuals, 4 to micro businesses and 3 to SMEs with 5 uncategorised. The ATO has also advised that between the 2011–12 and 2013–14 financial years, 42 per cent of freezing orders were subsequently amended by the court (21 per cent) and alternative undertakings were provided by the taxpayer (21 per cent).³⁸⁴

IGT observations

- 4.66 Given the level of risk involved in these cases, it is common for freezing orders to be sought without notice to the taxpayer. For this reason, and given the level of imposition on the taxpayer, the court commonly requires the Commissioner to provide undertakings with respect to damages where assets are improperly frozen at the behest of the ATO.
- 4.67 Furthermore, the period which taxpayers are unaware of the imposition of freezing orders is commonly restricted to one or two days after which they have an opportunity to be heard by the court as to whether the freezing order should be maintained (the onus, however, is on the ATO). Accordingly, the IGT believes that it would be inappropriate for the ATO to be required to provide notice to taxpayers where it intends to freeze assets as it would largely defeat the purpose of such notices and the court already has in place strong measures to ensure the Commissioner does not apply for inappropriate freezing orders.
- 4.68 Once a freezing order has been imposed, the IGT supports the ATO remaining open to engage with the taxpayer in an attempt to come to a satisfactory alternative arrangement, such as taking security over assets or providing undertakings to the court.
- 4.69 It is important that freezing orders are case managed by accountable staff to ensure that the relevant officer is fully informed of the circumstances of the case and is able to make decisions as to whether alternative arrangements are appropriate and respond to changing circumstances. Furthermore, taxpayers should be provided with appropriate contact details for the ATO officer managing their case so that proper discussions can be had and not with officers with no knowledge of the matter. Accordingly, the ATO should develop more comprehensive procedures with respect to freezing orders to ensure that management expectations are known and followed.

³⁸⁴ ATO, Communication to the IGT, 5 March 2015.

Departure Prohibition Orders

- 4.70 Stakeholders have raised concerns with the ATO's use of DPOs to restrict their movement. They are particularly concerned, where taxpayers may be unaware or uninformed that they have tax debts outstanding until the ATO has issued a DPO. The significant costs of DPOs, particularly on foreign residents have also been noted by stakeholders.
- 4.71 Stakeholders were also concerned that the ATO did not take into account taxpayers' circumstances. For example, in one case provided in submissions, the ATO had issued a DPO to a taxpayer who required urgent travel overseas for family commitments. Despite attempts to engage with the ATO to provide security for the disputed debt as well as assurance of their return to Australia, the ATO's delay in responding created considerable anxiety and distress for the taxpayer.
- 4.72 Stakeholders have called for greater external control on the ATO's use of DPOs, particularly during the course of disputes. A number of suggestions have been proffered in this regard, including that the ATO should be restrained from issuing DPOs where there is a challenge to the underlying debt or that the ATO should be required to seek judicial approval before DPOs are issued as they are required to do when seeking to freeze taxpayer assets.
- 4.73 The ATO's use of DPOs has also been the subject of judicial review³⁸⁵ and has attracted substantial media attention in relation to high profile taxpayers.

ATO materials

- 4.74 The ATO's approach to DPOs is outlined in Practice Statement PS LA 2011/18 and was described in Chapter 1. The practice statement acknowledges that DPOs impose a significant restriction on the normal rights of a taxpayer's freedom of movement and requires that there be 'reasonable grounds' for preventing the taxpayer from leaving Australia without discharging or making satisfactory arrangements to discharge their tax liability. The ATO will consider all relevant factors, such as whether a taxpayer is dissipating assets or moving them overseas and there are indications of overseas travel without good reason.
- 4.75 Although a DPO may have been issued, the Commissioner may authorise departure by issuing a DAC where he believes that the taxpayer will return to Australia within a reasonable time period, acceptable security has been provided by the taxpayer or there are humanitarian reasons to do so.³⁸⁶
- 4.76 Following the issuing of a DPO, regular reviews are undertaken to ensure that keeping the DPO in force is still appropriate or requires variation. Such reviews occur monthly by the case officer and quarterly with the relevant EL2 officers which takes into account any changes in the circumstances that warranted the issuing of the DPO and any additional factors or risks to revenue.³⁸⁷

³⁸⁵ *Pattenden v Commissioner of Taxation* [2008] FCA 1590.

³⁸⁶ ATO, 'Enforcement Measures', above n 56, paras [134]-[135], [137], [140]-[141].

³⁸⁷ Ibid, paras [151]-[152], [154]; ATO, 'DPO Guidelines', above n 93.

- 4.77 The ATO's authorisation guidelines state that officers at the EL2 and SES levels may make decisions to issue, vary or revoke DPOs. However, other ATO materials state that a decision:
- to issue a DPO or refuse to revoke a DPO may only be made by SES officers; and
 - to revoke a DPO may be made by an EL2 officer.³⁸⁸
- 4.78 The ATO conducted an internal review in 2012 of 38 active DPOs following findings of the Commonwealth Ombudsman relating to procedural matters. The aim of this review was to:
- ensure that all active DPOs were appropriate and if not proactively revoke them;
 - ensure that taxpayers who had an active DPO are aware of the ATO's reasoning for issuing the DPO and their review and appeal rights;
 - proactively identify any procedural gaps; and
 - provide assurance the procedures were fair and appropriate.³⁸⁹
- 4.79 Whilst the review found that the all decisions to issue DPOs were reasonable, the following improvement areas were also identified:
- The quarterly reviews of DPOs by EL2 officers only required them to simply confirm whether an update is required, they are familiar with the relevant taxpayer's circumstances and they are satisfied the DPO should be retained or the DPO should be revoked. No other reasoning was provided. It was proposed to require EL2 officers to provide reasons as to their decisions.
 - The template used to document an EL2's review of a decision not to issue a DAC was insufficient and required updating, for example, to include a chronology of the debt strategy and highlight what action has been undertaken since the issue of the DPO.
 - ATO officers were provided with two procedures by which to seek guidance on acceptable security when taxpayers apply for a DAC. There was a risk that case officers did not demonstrate a sound understanding or include relevant commentary on the level of acceptable security and the reasons for it. It was recommended to provide further guidance on determining acceptable security.
 - The majority of DPOs were issued with respect to Project Wickenby cases, however, consultation with the DBL through case callovers had ceased. These joint callovers were considered to provide a level of detail and accountability with the management of cases moving forward, particularly where the taxpayer had lodged an objection to the tax liability. Not re-instating the joint callovers would also risk losing sight of the broader direction and strategy of the case in the overall taskforce intent. Furthermore, a decision to maintain or remove a DPO would be enhanced by these discussions. Accordingly, re-instating the joint callovers was recommended.

388 ATO, 'Taxation Authorisation Guidelines', above n 75, para [1.5.1]; ATO, 'DPO Guidelines', above n 93.

389 ATO, 'Report - Departure Prohibition Order Review' (Internal ATO document, April 2012) p 3.

- Given the administrative deficiencies found by the Commonwealth Ombudsman, it was recommended that authorisations to issue DPOs be increased from the EL2 level to SES level officers to maintain manual assurance of DPOs.³⁹⁰

4.80 The below table shows the total number of DPOs initiated between 2011–12 and 2013–14. The market segment break-ups for DPOs are not available.

Table 4.4: Number of DPOs

	2011–12 (number of cases)	2012–13 (number of cases)	2013–14 (number of cases)	Total (number of cases)
Issued	4	1	4	9
Active DPOs	30	16	11	–

Source: ATO.

4.81 Table 4.4 above shows that the ATO had issued a total of 9 DPOs between 2011–12 and 2013–14. It also appears that the ATO has reduced its stock of active DPOs over this period from 30 to 11.

IGT observations

4.82 The issuing of a DPO is a severe action as it restricts a taxpayer's freedom of movement³⁹¹ and may have significant impacts, particularly for foreign residents. In this respect, DPOs are similar to freezing orders.

4.83 There is an important difference between DPOs and freezing orders. Freezing orders are determined by the judiciary and the ATO has the burden of proof to convince the court that such orders are appropriate. The ATO is also required to provide undertakings with respect to damages if the freezing order is later determined by the court to be inappropriate. DPOs, however, are an administrative instrument issued by the ATO. Additionally, whilst a taxpayer may appeal a DPO to a Supreme Court or the Federal Court of Australia, the taxpayer has the burden of proof to show that the DPO was wrongly made. Moreover, there are no similar taxpayer protections where DPOs are later determined to be inappropriate.

³⁹⁰ Ibid, pp 8–14.

³⁹¹ *Poletti v Deputy Commissioner of Taxation* (1994) 52 FCR 154, 160; *Edelsten v Commissioner of Taxation* (1992) 92 ATC 4285, para [20] (Northrop J); Attorney General, *Right to Freedom of Movement* <<http://www.ag.gov.au>>.

- 4.84 The IGT also observes that the ATO uses DPOs infrequently. Accordingly, it would be a difficult task for the ATO to maintain strong capability on the use of DPOs. Therefore, given the infrequency of their use, severity and potential risk to reputation, such decisions may more appropriately be made by the judiciary, similar to applications for freezing orders, as recently recommended by the House of Representatives Standing Committee on Tax and Revenue³⁹². However, whilst the Government considers this recommendation, the ATO could require approval by the Second Commissioner of the LD&P Group before DPOs are issued. This would also address the confusion as to the current authorisation process as noted above. In relation to the maintenance of DPOs, this should be done by appropriate SES officers rather than leaving it to more junior officers.
- 4.85 Once again, similar to freezing orders, DPOs should be case managed by accountable officers where disputes are involved. This will ensure that officers are fully aware of any changing facts which may impact the continuing appropriateness of the DPO and take quick action in response. Accordingly, case officers should continually monitor cases and where material information is found which may impact a DPO, escalate the matter for immediate consideration.

RECOMMENDATION 4.3

The IGT recommends that the ATO amend its processes for issuing Departure Prohibition Orders to require Second Commissioner approval and that SES officers be ultimately responsible for the maintenance of DPOs.

ATO response: Agree in Principle

The ATO agrees to consider the appropriate level of approval for Departure Prohibition Orders.

The ATO notes the existing authorisation [Senior Executive Service (SES) Band 1 within the Debt Business Line] is consistent with other Australian Government Agencies with similar administrative powers who have set their approvals to designated Executive Level 2 and SES Band 1 officers within their equivalent (Debt) areas.

Security over assets

- 4.86 Certain stakeholders have raised concern that the ATO has required taxpayers to provide disproportionate security in lieu of immediate payment of tax debts. For example, in one case provided, the ATO had taken security over all properties held by the taxpayer. Such terms were considered to be unfair and detrimental to the taxpayer.

³⁹² House of Representatives Standing Committee on Tax and Revenue, Parliament of Australia, *Tax Disputes* (2015) pp 36-40.

ATO materials

- 4.87 The circumstances in which the ATO may take security over assets were outlined in Chapter 1.³⁹³
- 4.88 In determining the quantum of security required, the ATO will consider the amount of the tax debt outstanding or expected future debts, including any estimated additional charges for late payment. Whether security is required commensurate to the full value of tax liabilities or a proportion of those liabilities will depend on the taxpayer's ability to provide that security and the taxpayer's compliance history amongst other things.³⁹⁴ Additional security from the taxpayer, however, may be required where there is a real risk of asset dissipation or evidence of rapidly escalating debt.³⁹⁵
- 4.89 In taking security, the ATO will aim to specify the amount of the security over the asset so that there is no uncertainty in law.³⁹⁶
- 4.90 The ATO has advised that as the decision to take security over assets is pursuant to its general powers of administration, no specific delegations or authorisations are needed to make such decisions. Furthermore, whilst not formalised, a practice has evolved where EL2 officers or above approve decisions to take security.³⁹⁷
- 4.91 Table 4.5 below shows the number of cases for which the ATO has taken security between 2011–12 and 2013–14.

Table 4.5: Number of cases involving security over assets

Business segment	2011–12 (number of TFNs)	2012–13 (number of TFNs)	2013–14 (number of TFNs)	Total (number of TFNs)
INB	1	4	8	13
LGE	—	2	3	5
MIC	15	10	15	40
NFP	—	1	—	1
SME	4	5	9	18
Uncategorised	1	1	1	3
Grand Total	21	23	36	80

Source: ATO.

- 4.92 The table shows that the majority of security taken was in relation to micro businesses (40), SMEs (18) and individuals (13) between 2011–12 and 2013–14. Together, these taxpayer segments contributed to approximately 71 per cent of the total number of securities taken.

393 ATO, 'General Debt Collection Powers and Principles' above n 48, para [80].

394 Ibid, paras [84], [86], [106].

395 Ibid, para [106].

396 Ibid, para [84].

397 ATO, Communication to the IGT, 21 January 2015.

- 4.93 More detailed statistics provided by the ATO shows that during the month of August 2014, the ATO had a total of 64 cases in which security was taken, or being progressed, with a total value of \$268 million to cover \$659 million in tax debts (41 per cent per cent of the value of debts was secured). In 26 of these cases, tax liabilities were disputed. Only one case was reported where the ATO released security.³⁹⁸

IGT observations

- 4.94 The data provided by the ATO in the above section shows that on average, the ATO takes security at less than half the value of tax debts which they aim to secure. Accordingly, for the most part, it appears that the ATO's security requirements may not be unreasonable. The IGT acknowledges, however, that the data provided is limited and may not show unique cases where large amounts of security have been requested.
- 4.95 In this respect, the IGT believes that the ATO could better prevent the risk of disproportionate security being taken by ensuring that the supervision of such decisions is appropriate.
- 4.96 As described in Chapter 1, the taking of security over taxpayer assets is generally ancillary to primary debt recovery actions. Currently, there are no formal authorisations for the taking of security by officers. Accordingly, the ATO should ensure that the authorisation to take security is allocated to appropriately senior officers to improve the integrity of the process. There are pre-existing formal authorisations for primary debt recovery actions that are designed to suit a range of different circumstances. For example, where a DPO is issued as a debt recovery action and security is provided by the taxpayer to obtain a DAC issuance, the relevant authorisations for each action should be issued by an appropriately senior officer. Such an approach would also ensure that any creditor preference which the ATO obtains is appropriate in the event that the taxpayer subsequently becomes insolvent.
- 4.97 Furthermore, as stated in the earlier sections on DPOs and freezing orders, there can be important considerations which need to be taken into account by the case officers in high risk cases. Similarly, there is a need for case management by accountable staff to ensure that decisions are appropriate.

RECOMMENDATION 4.4

The IGT recommends that the ATO formalise the authorisations required to take security over assets and allocate these authorisations to appropriately senior officers.

ATO response: Agree

The ATO is developing an authorisations framework for Security of Assets. Authorisations will be aligned to appropriately-skilled senior officers.

398 ATO, 'Securities: Monthly Report' (Internal ATO document, August 2014).

Offsetting credits with debits

- 4.98 Stakeholders have observed that the ATO has inappropriately applied taxpayers' credit amounts to offset debits in a range of cases. These cases include offsetting PAYG Instalments, income tax refunds and Centrelink family tax benefits against pre-bankruptcy debts, disputed debts or liabilities not yet due.
- 4.99 In one example provided in submissions, the ATO had offset an instalment credit amount despite the taxpayer having an arrangement in place for the payment of their tax debt. The ATO then issued the taxpayer with a notice that they had not paid the correct instalment amount.
- 4.100 In other cases, stakeholders have observed that the ATO will not offset amounts and pursue a tax debt on one of the taxpayers' account where their other account is in credit.

ATO materials

- 4.101 The legislative requirement for the ATO to offset credit and debit amounts, the limited discretion not to offset those amounts and the general considerations taken by the ATO in doing so were described in Chapter 1.
- 4.102 Offsetting may also occur during disputes and where taxpayers are insolvent. For disputed tax debts, the ATO may exercise the discretion not to offset amounts until an objection is determined or withdrawn by the taxpayer. If the debt is subject to appeal and the taxpayer has entered into a 50/50 arrangement, the ATO will not offset amounts against the remaining balance of the disputed tax until the arrangement has expired. In appeal cases where a taxpayer has not entered into a 50/50 arrangement, the ATO will offset amounts up to the full extent of the taxpayer's liability.³⁹⁹
- 4.103 In relation to insolvent individuals, the ATO may continue to offset amounts. Only where the taxpayer becomes a 'discharged bankrupt', will debts become irrecoverable at law. Accordingly, any credits can be applied to reduce both pre and post sequestration liabilities in the meantime.⁴⁰⁰ The ATO will also offset amounts pursuant to any agreement made with the taxpayer. Any credits which are attributable to periods before an agreement was made, however, will be offset as required by bankruptcy law.⁴⁰¹ A similar approach applies with respect to companies in administration.⁴⁰²
- 4.104 Where offsetting occurs, the ATO has advised that it is processed in its systems through both automatic and manual methods.

³⁹⁹ ATO, 'Offsetting', above n 101, paras [35]-[38].

⁴⁰⁰ Ibid, paras [125]-[127].

⁴⁰¹ Ibid, paras [106]-[124].

⁴⁰² Ibid, paras [125]-[127].

- 4.105 Offsetting, as shown in the ATO's complaints for the 2013-14 financial year, has received the fourth highest number of all complaints (242 or 6.5 percent of all complaints).⁴⁰³

IGT observations

- 4.106 As noted above, offsetting is permitted in insolvency, pursuant to any debt agreement. In this respect, the ATO has processes for staff which direct them as to how amounts are offset in insolvency. However, as noted in Chapter 1, junior ATO staff may make such decisions. Accordingly, the IGT believes that appropriate supervision of ATO staff would help ensure that correct amounts are offset pursuant to any agreement. Better supervision would also help ensure that appropriate decisions were made in relation to offsetting amounts where debts are not yet due.
- 4.107 The IGT also observes that the guidance given to staff on offsetting credits in situations other than insolvency (where the Offset Criteria described in Chapter 1 are met) does not inform ATO staff that the ATO has a discretion to *not* offset credits against debts.⁴⁰⁴ As a result, there is a risk that ATO staff may not fully inform taxpayers of this discretion where it may be important for maintaining their ongoing business performance and viability. Accordingly, the IGT believes that the ATO's staff guidance should be expanded in this regard. Practically, this has the effect of overriding the default position which is to offset credits against debts.
- 4.108 In relation to offsetting which may occur during disputes, whilst there is a need for the ATO to quickly recover tax debts (as the longer a debt remains outstanding, payment risk increases), care needs to be taken to ensure that the recovery does not frustrate taxpayers' abilities to put forward their best case in disputes. Accordingly, the IGT believes that consideration of whether to exercise the Commissioner's discretion not to offset tax debts for disputed debts should occur concurrently with, and on the same basis as, his decision as to whether to accept a 50/50 arrangement. This could also then form part of the discussions between the compliance, debt and legal business lines.
- 4.109 The existence of payment arrangements also does not mean that the ATO will not offset amounts as the ATO is not obliged to exercise the discretion. Accordingly, this may result in offsetting amounts despite the existence of payment arrangements. The IGT believes that where a taxpayer is negotiating a payment arrangement with the ATO, discussions should include whether the discretion to *not* offset should be exercised. This would enable more comprehensive payment discussions to be had which can better take into account taxpayer's circumstances.

403 ATO, 'Debt Ministerials and Complaints', above n 176, p 3; ATO, Communication to the IGT, 18 November 2014.

404 ATO, 'SMART: Payment plan conditions' (Internal ATO document, 8 January 2015).

- 4.110 Furthermore, where the discretion to *not* offset is exercised, taxpayers should be informed that they are permitted to request otherwise. This approach has a number of benefits. Taxpayers may prefer offsetting which would also allow the ATO to recover tax liabilities sooner. It would also address issues where the ATO pursues debts when taxpayers have other accounts in credit. The IGT believes that whilst the ATO does in practice allow taxpayers to request offsetting, better notification and communication of the mechanism is needed. For example, in addition to the payment arrangement negotiation process noted above, the ATO could also provide such notice in its written confirmation of payment arrangements.

RECOMMENDATION 4.5

The IGT recommends that, where the criteria for offsetting credits against debts are met, the ATO provide guidance to staff to inform taxpayers of their right to request the discretion 'not to offset' be exercised at the outset of discussion relating to, for example, disputed debt or payment arrangements.

ATO response: Disagree

As noted in paragraph 4.101 of this report, offsetting credits against debits is a legislative requirement. This, in the main, happens automatically as part of our accounting system. Practice Statement Law Administration (PS LA) 2011/21 states there are limited circumstances where the Commissioner may decide not to offset, but refund a credit instead:

1. where it is not yet due - this refund happens automatically therefore there is no need for guidance for staff; or
2. where recovery action is deferred (for example where there is a dispute). Existing guidance prompts staff to advise the taxpayer how they can request a refund in this circumstance. This advice is reiterated in the 50/50 Payment Arrangement letter issued to the taxpayer; or
3. where a taxpayer is complying with a Payment Arrangement. During arrangement negotiations the ATO takes into account the taxpayer's account history, stated financial position and personal circumstances. This includes the likelihood of any credits arising during the period of their proposed arrangement. The taxpayer is advised during the negotiation that any credits will be automatically offset whilst there is a debt outstanding. This ensures the ATO collects revenue within the shortest period possible and benefits the taxpayer by reducing the amount of General Interest Charge applied.

Where the offsetting of a credit would cause serious financial hardship, taxpayers can contact the ATO to request a refund, as advised on the ATO's website. Existing procedures guide staff to manage requests from taxpayers experiencing financial hardship who are requesting their credit not be offset to an existing debt.

Insolvency action

- 4.111 Stakeholders have questioned whether the ATO's insolvency policy is based on qualitative rules (such as the existence of certain facts) as they are considered to result in better outcomes than simply quantitative thresholds (such as, accepting agreements based on receiving a certain percentage) which may be manipulated by taxpayers.
- 4.112 Where the ATO has commenced insolvency action it appears to take an aggressive approach. For example, stakeholders have observed that the ATO has:
- issued garnishee notices before insolvency proceedings to get payment preference against other creditors;
 - not voted in favour of Deeds of Company Arrangements (DOCA) and personal debt agreements;
 - taken a threshold approach to voting;
 - assessed the value of DOCAs and pushed for liquidation before other creditors have the chance to vote; and
 - disregarded other creditors' circumstances.
- 4.113 Certain stakeholders have also observed that liquidators have spent significant amounts of money (which reduces the amount available for distribution) to defend against the ATO in the above circumstances.
- 4.114 Stakeholders have also observed that during insolvency, the ATO does not provide trustees in bankruptcy with the same level of access to a taxpayer's information as it affords to company liquidators. In one example, this had occurred despite notices issued by the Official Receiver which are intended to overcome such difficulties. Stakeholders also believe that more effective ATO recovery action could be taken before pursuing legal avenues as the extent of the dividend return attributable to insolvency is minimal. The IGT has considered the need for earlier and more frequent action in this regard in Chapter 2.

ATO materials

- 4.115 The ATO's approach to deciding whether to take insolvency action as well as voting on DOCAs and personal debt agreements was described in Chapter 1.
- 4.116 In relation to the issuing of garnishee notices in particular, the ATO's Practice Statement PS LA 2011/16 states that valid garnishee notices, issued before insolvency action, will generally not be withdrawn simply because a representative of an incapacitated entity⁴⁰⁵ has been appointed. However, such notices must be issued prior to wind up to remain effective and at least 6 months before a bankruptcy petition.⁴⁰⁶

⁴⁰⁵ Incapacitated entity is defined to mean an individual who is a bankrupt, an entity that is in liquidation or receivership, or an entity that has a representative: ATO, 'Insolvency - Collection' above n 60, para [97].

⁴⁰⁶ ATO, 'Insolvency - Collection' above n 60, para [136]-[140].

- 4.117 On the provision of information to trustees in bankruptcy, Practice Statement PS LA 2011/16 states that, generally any disclosure of information which is authorised by the confidentiality provisions in Division 355 of Schedule 1 to the TAA 1953 will be authorised for the purposes of the *Privacy Act 1988*.⁴⁰⁷ Specifically, it is recognised that representatives of incapacitated entities need to investigate the affairs of insolvent entities (for example, trustees in bankruptcy for bankrupt individuals) and may need to access information held by the ATO to fulfil their role.⁴⁰⁸
- 4.118 Such information, however, should be relevant to the administration of the incapacitated entity or their taxation affairs. The level of information provided will be dependent on the role of the representative. For example, where there will be a dual responsibility for an entity's affairs (both the taxpayer and their representative in bankruptcy), tax officers will need to consider whether the information requested by the representative is relevant to the administration of the entity's insolvency.⁴⁰⁹
- 4.119 Where it is unclear that the information can be given without breaching confidentiality provisions, staff are directed to seek advice in the first instance from the Operational Policy, Assurance and Law unit.⁴¹⁰

IGT observations

- 4.120 The ATO's policy in relation to taking insolvency action and whether to agree to debt agreements or arrangements are largely based on quantitative assessments, such as the taxpayer's asset position and whether the taxpayer has been trading whilst insolvent, the quantum of debt and the relative cost of action compared to the likely return. However, there are also qualitative considerations, such as whether taxpayers have made arrangements to pay debts, were involved with potential criminal activity or otherwise improperly sought to alienate assets. The IGT considers that a policy which considers both quantitative and qualitative aspects is appropriate as it should result in well-considered decisions. However, as noted in Chapter 1, junior ATO officers are authorised to initiate insolvency proceedings and accept debt agreements or arrangements. Accordingly, there is a need for better supervision to ensure that decisions are appropriate before they are made, such as approval by more senior officers (for example, EL2 officers). The IGT believes that such assurance would address many of the stakeholders' concerns with the ATO's approach during insolvency actions. The need for better supervision is further discussed later in this chapter.

⁴⁰⁷ Ibid, para [134].

⁴⁰⁸ Ibid, paras [95]-[97], [126].

⁴⁰⁹ Ibid, para [127].

⁴¹⁰ Ibid.

- 4.121 Specifically, whilst the ATO is entitled to issue garnishee notices before insolvency action, the impact on the other creditors of the taxpayer needs to be considered. This is because the issuing of garnishee notices in these situations effectively elevates the ATO's claim above other creditors. Such an outcome has the potential to cause additional financial distress for other creditors. As noted in Chapter 2, the IGT believes that the ATO needs to consider the impact of its actions on the broader economy. In this respect, the IGT observes that the ATO procedures only require such matters to be considered once a company receiver is appointed, however, it is unclear whether a similar consideration occurs leading up to insolvency or when the ATO votes on DOCAs and personal debt agreements. Accordingly, the ATO should amend its procedures to ensure that staff consider the impact on other creditors, including when voting on debt agreements and arrangements.
- 4.122 Furthermore, as stated in previous sections, there is a need to ensure that all insolvency actions are case managed by accountable staff particularly where debts may be disputed. This would ensure that appropriate decisions are made by fully informed staff in relation to these cases as well as ancillary activities, such as whether the issue of a garnishee is appropriate.
- 4.123 Lastly, the ATO's practice statement recognises the role of trustees in bankruptcy and will provide information where it is relevant to the administration of the taxpayer or their taxation affairs. Staff are also directed to seek advice if they are unsure about providing the information. There are also corresponding staff procedures within its SMART system. Accordingly, to better ensure that its procedures are being followed, there is a need for improved compliance, supervision and training which is discussed later in this chapter.

RECOMMENDATION 4.6

The IGT recommends that the ATO incorporate into its procedures and guidance the need to consider the impact of its actions on other creditors as it pursues tax debts.

ATO response: Agree

Known information about other creditors is taken into account in our decision making processes where appropriate, particularly when considering the financial position of the taxpayer.

The ATO is required by the Public Governance, Performance and Accountability (PGPA) Act and Framework, and Corporations Act 2001 to take timely action to address outstanding debts where we have concerns about solvency.

Through our more timely and appropriate action, we will ensure debts are not escalating beyond control and businesses are not getting an unfair financial advantage.

Collection of disputed debts

- 4.124 Stakeholders have observed that many taxpayers do not fully appreciate that, unlike private sector creditors, the ATO is permitted to recover debts arising from disputed liabilities notwithstanding that the dispute is unresolved.⁴¹¹ Taxpayers are also generally not cognisant of disputes and recovery of taxes being separate processes.
- 4.125 Stakeholders also consider that the ATO's requirements for a 50/50 payment arrangement to stay recovery action arduous, particularly where there is no or little payment risk. They consider that these requirements can have a significant impact on taxpayers' abilities to effectively challenge the ATO's decisions.
- 4.126 Furthermore, stakeholders have observed that when deciding whether debt recovery action should be stayed, there is a disconnect between ATO legal officers, who better understand the technical issues involved, and debt officers.

ATO materials

- 4.127 The ATO's approach to disputed debts, the use of 50/50 arrangements and the interface between debt and compliance business lines were described in Chapter 1.
- 4.128 The ATO has advised that the Debt Case Leadership (DCL) unit will attend case callovers with the relevant compliance unit where there is a significant compliance, revenue or reputation risk. The callovers may also include other participants from the SDM unit or RDR business line from the LD&P Group. The aims of these callovers are to:
- improve the collection of debts through a greater focus on resolution and working with the taxpayer to resolve issues and disputes prior to the raising of an assessment;
 - develop strategies to deal with the progress of audits with existing debt as well as to minimise the risk to revenue and reputation; and
 - provide updates, advice, assistance and share intelligence.⁴¹²
- 4.129 For significant cases, the ATO also establishes cross business line steering groups which involve SES officers, including Deputy Commissioners, to provide oversight of the approach taken.⁴¹³
- 4.130 The ATO has also advised that a recurring taxpayer complaint is not being able to discuss their concerns with an ATO debt officer once litigation action had commenced and a legal representative appointed. The ATO's Debt Ministerials and Complaints unit has since consulted with the Formal Recovery unit which resulted in the RDR business line providing guidance to staff to assist them with managing these enquiries.⁴¹⁴

411 *Deputy Commissioner of Taxation v Broadbeach Properties Pty Ltd* [2008] HCA 41.

412 ATO, Communication to the IGT, 2 March 2015; ATO, 'Recovery of Debts of a Significant Nature' (Internal ATO document, 10 November 2014); ATO, 'Overarching Principles', above n 130.

413 ATO, Communication to the IGT, 2 March 2015.

414 ATO, Communication to the IGT, 18 November 2014.

IGT observations

- 4.131 The law allows the ATO to recover taxes before disputes are resolved so that the dispute cannot be used as a means to frustrate the collection of tax that is properly payable.⁴¹⁵
- 4.132 Whilst there is a need for the ATO to quickly recover tax debts, care needs to be taken to ensure that the recovery does not frustrate a taxpayer's ability to put forward their best case during a dispute. For example, whilst taxpayers can initiate dispute proceedings in either the AAT or the Federal Court, the ATO may concurrently initiate debt recovery proceedings in state courts.
- 4.133 To defer recovery proceeding, the ATO may require the taxpayer to enter a 50/50 arrangement. Although less onerous than full upfront payment, 50/50 arrangements may still have a significant impact on a business' viability and the ability to challenge assessments, particularly as there may be limited access to funds. The resulting pressures on businesses may be excessive, especially where the ATO issues protective assessments which require taxpayers to prove the correct liability.
- 4.134 In other jurisdictions, such as the United States⁴¹⁶ and Ireland,⁴¹⁷ debt recovery activity is not commenced until disputes are resolved. If disputes are resolved in the revenue authority's favour, interest is payable on any outstanding tax. Such an approach in relation to debts arising from primary tax⁴¹⁸ has the potential to encourage frivolous disputation. A more graduated approach which appropriately reflects, amongst other things, a taxpayer's payment risk, the merits of their dispute, their compliance history and the quantum of disputed debt, may be more appropriate. There are current ATO system limitations which prevent such an approach and the ATO believes that the different grades of risk may themselves become a source of disputation.⁴¹⁹ However, there may be merit in exploring such an option.

415 *Taxation Administration Act 1953* ss 14ZZM, 14ZZR.

416 In the US an assessment of tax does not occur until disputes are resolved and collection activity occurs after such an assessment.

417 In Ireland, legislation specifically defers collection activity until disputes are resolved: Section 934(6) and 941(9) *Tax Consolidation Act 1997*.

418 IGT had previously recommended that the ATO not require taxpayers to pay penalty amounts until disputes are resolved, to dispel perceptions of penalties being used as leverage in primary tax disputes and to relieve the financial pressure on taxpayers: IGT, 'Penalties review', above n 120, para [2.49], Recommendation 2.2.

419 ATO, Communication to the IGT, 5 December 2014.

- 4.135 In relation to the disconnect between debt and compliance units, as mentioned throughout the earlier sections of this chapter, the IGT considers that it would be difficult for debt officers to apprise themselves of the facts and technical issues underlying the tax liabilities. Such knowledge is held by compliance or legal officers who are involved in related audits or disputes. However, such an understanding is often necessary for debt officers so they make appropriate decisions in the recovery of disputed debts. Better interaction between compliance, legal and debt officers could facilitate the necessary knowledge transfer to enable more informed recovery strategies and holistic engagement with taxpayers, including being more responsive to taxpayer attempts to re-engage as noted in the IGT's *Review into Aspects of the Tax Office's Settlement of Active Compliance Activities*.⁴²⁰
- 4.136 An integrated approach was supported by the OECD in relation to Sweden's 'payment thinking' which requires all staff to be aware of the potential payment difficulties at the conclusion of compliance processes and that action is taken as soon as possible thereafter if there is a risk that payment will not be made. This means that compliance management be involved in devising a strategy to diminish the payment risks.⁴²¹ It was noted in Chapter 1 that the ATO had implemented such actions and developed improved staff guidelines across the Compliance Group.⁴²² Such an approach is embedded in processes for high risk cases, however, for the low risk cases there is a risk that taxpayers' concerns with liability issues may not be appropriately addressed if debt officers are not responsive to these issues during collection processes. The IGT has commented and made recommendation on this point in relation to garnishee notices earlier in this chapter.
- 4.137 In the IGT's view, requiring debt, compliance and legal officers to consult on debt recovery strategies for cases would reduce taxpayers' compliance costs and more accurately assess the risk of non-payment as it would more effectively make use of the knowledge of the taxpayer's circumstances and the ATO's debt recovery expertise in developing recovery strategies. The ATO's current joint callover process is generally limited to higher risk or higher value cases. Moreover, it may not result in the most efficient or streamlined approach as multiple ATO groups are involved.
- 4.138 The IGT has previously raised the benefits of transferring the DBL into the Compliance Group of the ATO.⁴²³ The ATO statistics suggest that liabilities arising from compliance activities (for example, \$15.2 billion in 2013-14) are less likely to be paid on time (\$9.4 billion in 2013-14) at 62 per cent compared with 89 per cent for all tax liabilities.⁴²⁴ The IGT believes that the transfer of the DBL would result in a more efficient and streamlined approach. Whilst it could be argued that not all debts result from compliance activities and disputes, debts are essentially a (payment) compliance issue which also has synergies with lodgment compliance. Additionally, the ATO's new debt strategy demonstrates evolution towards a compliance focus, such as use of the RDF. Accordingly, the next step in the evolution of the DBL could be a move into the Compliance Group which the ATO should explore.

420 IGT, *Review into Aspects of The Tax Office's Settlement of Active Compliance Activities* (2009) pp 29-30.

421 OECD, 'Tax Debt Management', above n 45, p 36.

422 ATO, 'Tier 3 Closure Report' above n 132.

423 IGT, *The Management of Tax Disputes* (2015) pp 95-96.

424 Commissioner of Taxation 'Annual Report 2013-14', above n 35, p 46; ATO, 'Debt Strategy 2014-18', above n 42.

RECOMMENDATION 4.7

The IGT recommends the ATO consider merging the Debt Business Line into the Compliance Group.

ATO response: Disagree

The ATO is committed to providing timely, tailored advice and services that make it easier for taxpayers to get tax and superannuation right. The appropriate organisational structure to achieve this will be considered and determined through our Reinvention program.

SUPERVISION AND CASE MANAGEMENT OF DEBT RECOVERY ACTIVITIES

- 4.139 A common theme observed in stakeholder concerns with respect to the ATO's firmer debt recovery activities in the sections above, was the need for better supervision of the very junior staff who make significant debt-related decisions. Stakeholders were concerned that the ATO's debt strategies and processes were not being effectively implemented.
- 4.140 Stakeholders have also commented that the current approach to case management was ineffective for two reasons. First, stakeholders have been unable to find ATO officers to discuss tax debts, including some supervisors to whom matters are escalated. Secondly, stakeholders have also found it difficult in complex cases to deal with the ATO due to many different officers having responsibility for different aspects of the case. This is said to result in further costs and issues for taxpayers, such as subsequent lodgment delays and associated penalties until issues are resolved.

ATO materials

- 4.141 Chapter 1 explained the ATO's approach to the case management of particular debt recovery activities depends on the particular unit which is taking the action.
- 4.142 The ATO has advised that it has mechanisms to ensure that practices, procedures and guidance in relation to debt activities are followed by debt officers. These mechanisms are:
- system and access controls;
 - quality and coaching frameworks;
 - a 'product function'; and
 - tax authorisations for staff.
- 4.143 Each of the above mechanisms listed will be described in further detail in the sections below.

System and access controls

- 4.144 The ATO has advised that access to particular tax administration functions are controlled through security designations which are assigned to staff in employee management systems, organisation unit information and taxpayer record security attributes. All three requirements must align before staff members can conduct certain work.⁴²⁵

Quality and coaching frameworks

- 4.145 During the review, the ATO was in the process of transitioning from the Debt Quality Management System to a Service Delivery Quality Management System (SDQMS) which will be used across the entire SDSP.⁴²⁶
- 4.146 The new SDQMS borrows from the previous quality system. However, the new system is expected to provide an outcome-based assessment approach which focuses on the impact of interactions. This effectively requires an assessment of whether a suitable or appropriate outcome was achieved for both the taxpayer and the ATO.⁴²⁷ Towards the end of this review, ATO management made representations to the IGT that the DBL has implemented a national moderation process, which included quality assessors and team leaders focus on consistency in assessment and coaching of staff.⁴²⁸
- 4.147 The SDQMS is also geared towards developing staff capability through a coaching and performance framework. This framework is intended to provide a consistent approach to coaching and managing performance across the SDSP to improve performance and develop staff capability through regular coaching between managers and team members.⁴²⁹

Product function

- 4.148 The ATO has advised that reviews are undertaken to assess the effectiveness of process, procedures and systems against the law, the ATO's administrative practices as well as taxpayer expectations.⁴³⁰ The outcomes of these reviews are assessed on a risk basis and systems change management, procedural change or external communications, may be required as a result of the reviews.⁴³¹

⁴²⁵ ATO, Communication to the IGT, 12 January 2015.

⁴²⁶ ATO, Communication to the IGT, 18 November 2014.

⁴²⁷ Ibid.

⁴²⁸ ATO, Communication to the IGT, 1 April 2015.

⁴²⁹ ATO, 'Service Delivery - Quality Management and Performance' (Internal ATO document, 2014); ATO, Communication to the IGT, 18 November 2014.

⁴³⁰ ATO, Communication to the IGT, 12 January 2015.

⁴³¹ Ibid.

Authorisations, capability and work allocation

- 4.149 ATO staff can only make decisions on the type of recovery action to take and with respect to the quantum of debt for which they have been authorised. The authorisations were outlined in the relevant sections in Chapter 1. Overlaying these authorisations is the ATO capability requirements of its staff which depends on the type of work they perform.⁴³²
- 4.150 The ATO has advised that for staff, who operate in a call centre type environment, who mainly undertake 'early collections' work, there are two levels of capability. These levels are 'consolidating' their knowledge and 'proficient'. Proficiency is signed off by the team leader who reviews the officer's work, including listening to their phone conversations with taxpayers.⁴³³
- 4.151 For staff undertaking 'firmer action' work, team leaders may establish structures around the types of work that team members complete. For example, team leaders may allocate work based on officers' level of expertise or give officers extra support, such as through a 'buddy' system. The ATO has advised that the absence of rules is due to the fact that the level and types of support will vary between individuals and between work types. However, in general terms and as mentioned in Chapter 3, the ATO applies a 'one-third' ratio of the relevant training product to be spent with a buddy.⁴³⁴
- 4.152 Generally, once an officer is deemed 'proficient', their work is no longer overseen unless a pre-decision quality check is required by procedures or the DCL unit is involved. The DCL unit deals only with the higher end of significant debt management issues and complex cases.⁴³⁵ Staff, however, have access to support mechanisms, such as coaching assistance and access to team leaders. Towards the end of this review, ATO management made representation that it now aims to update the support mechanisms for staff. These support mechanisms are shown in Appendix 8.
- 4.153 The ATO has advised that it had developed a Debt Skill Model in 2013 and is currently developing a new capability framework which will act as a single repository of skills expected at different APS levels as well as details of officers' current capabilities which will apply across the SDSP. The expected capabilities will be benchmarked accordingly to the skills of a 'professional debt collector'.⁴³⁶

432 ATO, 'Service Delivery: Transforming our Business', above n 174.

433 ATO, Communication to the IGT, 9 December 2014.

434 Ibid; ATO, Communication to the IGT, 19 November 2014; ATO, 'Debt Skill Set Model', above n 303.

435 ATO, Communication to the IGT, 9 December 2014.

436 Ibid.

- 4.154 The ATO has also advised that particular types of debt work are assigned to staff based on their capability. For staff undertaking early collections work, cases are assigned based on the training they have completed. This occurs through a matching process of the training system to the work allocation system. For staff undertaking firmer action work, cases are allocated through case management systems to particular teams rather than specific officers. Team leaders will then allocate cases based on the skills of their team members. This is because the case management systems cannot be configured for a particular officer's skill set unlike those used for early collections work. The ATO aims, however, as part of a new capability framework, to be able to allocate work based on the 'skills profile' of its debt staff (capability matrix). Such functionality is currently not operational.⁴³⁷
- 4.155 Whilst the ATO aims to ensure that staff have sufficient capability, the ATO has advised, however, that it generally does not focus on ensuring consistency between the work of different teams.⁴³⁸

IGT observations

- 4.156 Debt recovery activity which is appropriate and consistent between taxpayers with similar circumstances better engenders voluntary payment over the longer term. Accordingly, there is a need to ensure that staff with the appropriate level of expertise and experience are handling debt cases and that they are adhering to procedures.
- 4.157 The ATO's development of improved quality and coaching frameworks to conduct real-time, outcome-based assessments of the end-to-end process is a positive step and may help prevent issues in future. The IGT notes that the ATO began the process of implementing these new frameworks during this review. Accordingly, the new frameworks may be better examined after the resulting changes have been implemented and bedded down.
- 4.158 Staff decision authorisations are another mechanism to help prevent real-time issues from occurring. Generally, the more severe the impact of the decision, the higher the authorisation required to make it. Comments and recommendations with respect to authorisation levels for specific debt recovery activities were discussed in the earlier sections of this chapter.
- 4.159 Overlaying the staff authorisations is a capability requirement. Whilst staff may be authorised to make certain decisions, unless they are 'proficient', they work in conjunction with a 'buddy' to guide decision making.
- 4.160 As mentioned before, unlike for early collection work, there is no similar work allocation for those conducting firmer action work. Instead, team leaders have discretion as to how they allocate and supervise work. Accordingly, the IGT supports the ATO's development of the capability matrix. The IGT believes that a more integrated system would better allow cases to be allocated to appropriate officers.

⁴³⁷ Ibid; ATO, 'Service Delivery: Transforming our Business', above n 174.

⁴³⁸ ATO, Communication to the IGT, 9 December 2014.

- 4.161 The IGT also observes that whilst staff have access to various support mechanisms, once they are deemed proficient, they may not be subject to any supervision and directed to seek assistance as necessary. The exception appears to be in relation to strategic recovery work where staff may interact with the DCL unit on the highest risk cases.
- 4.162 Accordingly, the IGT believes that there is a need for better ‘top-down’ supervision and ‘bottom-up’ advice or escalation for all staff regardless of their proficiency. This would allow, for example, ‘proficient’ staff to receive advice where needed and not be left to make uninformed decisions. For example, a consultant report found that whilst the ATO has taken positive steps towards the new strategy, it appeared that some officers had not entirely come to terms with the strategy, reverted back to the previous mindset and took enforcement action where it was perhaps not appropriate.⁴³⁹ In this respect, towards the end of this review, ATO management represented that it had recently developed a tool which aims to help team leaders identify and address skilling needs for DBL staff where taxpayers default after payment arrangements have been agreed.⁴⁴⁰ Whilst such a tool may be useful to identify skilling needs, it does not proactively ensure that appropriate decisions are made at the outset. Accordingly, there is still a need for better supervision of staff.
- 4.163 Furthermore, ATO officers may have limited access to previous quality decisions and precedents. Without access to such materials, ATO officers may be tempted to form their own perceptions of good decisions.
- 4.164 Accordingly, the IGT considers that the capture and dissemination of good decisions and associated reasoning, including the relevant facts and evidence relied upon, in an easily searchable database, would be invaluable to ATO officers. Such dissemination of corporate knowledge would assist existing and new staff to elicit principles and guide them towards better and consistent decision making.
- 4.165 Furthermore, examples of good decisions and precedents could be extracted and developed by utilising existing advisory ‘networks’ of experienced staff across the DBL who could provide advice as well as run workshops to help develop capability. This would also help promote the consistency of decisions between different teams which is currently not a focus for the ATO. It is recognised, however, that such systems must be feasible within a high case volume environment so as not to adversely impede the flow of work. In this respect, the ATO could include such work as part of the development of its coaching framework.
- 4.166 Effective case management of debt recovery activities may also help to ensure that appropriate debt recovery actions are taken, particularly as a taxpayer may have multiple interactions with different ATO staff in relation to their case.

⁴³⁹ An External Report.

⁴⁴⁰ ATO, Communication to the IGT, 1 April 2015.

- 4.167 Having a single officer accountable for the end-to-end process of a taxpayer's debt case would allow the officer to have a full appreciation of the case history and the taxpayer's circumstances. Such an appreciation would help ensure that decisions were fully informed, including escalation to more senior staff where necessary. An accountable officer would also create a single point for taxpayer interaction. Such an option may not be feasible in a low risk, high case volume environment due to limited ATO resources. However, the IGT believes that as the impact of the ATO's debt recovery increases, so does the need for case management by ATO staff who should have direct accountability for the case. This would help ensure that higher risk and disputed debt cases are being properly managed as identified throughout the earlier sections of this chapter.
- 4.168 For lower risk cases, where taxpayers attempt to engage with the ATO, better case management would ensure that staff contacted by taxpayers can direct their calls to those who have the authority and responsibility to discuss their concerns. Such a system relies heavily on the quality of information inputted by staff. However, as previously identified, internal ATO reports have found that staff, particularly in relation to lower risk cases, do not always make adequate records required within the case management systems. Therefore, the management of lower risk cases could be improved if systems were properly maintained.

RECOMMENDATION 4.8

The IGT recommends that the ATO:

- (a) improve Debt Business line team leader supervision of staff including requiring team leader approvals in appropriate cases;*
- (b) align case allocation systems with the debt staff capability matrix once developed;*
- (c) implement a network of advisory staff in the Debt Business Line to support escalation of issues, development of precedents and an effective database of debt decisions; and*
- (d) improve the enforcement of recording details of debt cases on its systems to promote better management of particular lower risk cases.*

ATO response: Agree

As outlined in the Reinventing the ATO Program blueprint, to bring our transformational change to life, our staff will be empowered and trusted to act and will have access to contemporary tools. Our people, already highly skilled and knowledgeable, will have further opportunities to broaden their knowledge. They will learn from the strong leaders around them, helping to build the capabilities needed to continue to meet the expectations of the community.

The ATO recognises the importance of an appropriate governance regime and we have built in quality assurance process and external review across a range of our processes.

To support effective decision making the ATO already:

- includes case studies within our Negotiation, Payment Arrangement, and Service Excellence training;
- undertakes monthly moderation of case decisions with coaches and team leaders who subsequently discuss these cases in team meetings with staff members; and
- has quality assurance processes that include formal and informal review of decisions, and provision of feedback to each staff member individually.

ATO CONDUCT AND COMMUNICATION DURING DEBT RECOVERY

4.169 Stakeholders have generally commented that as the majority of tax is voluntarily paid, reducing debt ultimately comes down to the effectiveness of contact with those taxpayers who are unable to pay or choose not to pay. However, stakeholders have observed that taxpayers are sometimes treated by ATO officers with indifference or are disproportionate in their behaviour. A few examples provided in submissions include:

- cases where taxpayers felt pressured to sign confidentiality agreements when matters were settled in their favour;
- a taxpayer being 'cautioned' by the ATO that if they appealed a summary judgment, the ATO would seek to recover significant costs;
- threatening warning letters with respect to penalties and interest as well as prosecution and imprisonment; and
- the ATO not acting like a 'model litigant' during litigation.

4.170 Stakeholders believe that disproportionate communication and engagement with taxpayers could intimidate them to unnecessarily self-initiate bankruptcy or voluntary administration.

4.171 Stakeholders have also made many observations which lead them to believe that it is futile to attempt to engage with the ATO as the ATO is unwilling to engage and does not communicate sufficiently. Such observations include the ATO:

- refusing to discuss disputed debts even where taxpayers proposed payment arrangements;
- not responding to taxpayers' questions which resulted in unnecessary firmer action;
- not disclosing payment assistance that may be available to taxpayers or communicating to taxpayers that debts treated as uneconomical to pursue will accumulate interest and may be subsequently re-raised;

- infrequent contact with taxpayers before taking firmer action; and
- refusing to communicate with registered tax agents in relation to their clients' debts and not informing them of their clients' debts, interest or penalty amounts causing difficulties for tax agents not having access to relevant information.

ATO materials

4.172 Broadly, the conduct of the APS is governed by section 13 of the *Public Service Act 1999*, which amongst other things requires APS employees to behave honestly and with integrity as well as to treat everyone with respect and courtesy. The ATO's *Taxpayers' Charter* outlines similar behaviours which taxpayers can expect from its staff. There is also a requirement for the Commonwealth to act as a model litigant.⁴⁴¹

4.173 As part of the new debt strategy described in Chapter 2, the ATO is developing a 'Debt Engagement Framework' to focus on re-engagement with taxpayers to help them understand and manage their payment obligations and deal effectively with any debt that arises.⁴⁴² Within the boundaries stated above in relation to expected ATO staff behaviour, this framework informs the ATO's approach in engaging taxpayers.⁴⁴³ In determining their approach to engaging with taxpayers, debt staff are required to consider:

- whether a taxpayer's debt is escalating over time;
- whether the taxpayer has a history of failed payment arrangements;
- the taxpayer's payment risk;
- the taxpayer's lodgment compliance; and
- the taxpayer's capacity to pay.⁴⁴⁴

4.174 Furthermore, as part of conversations with taxpayers, ATO staff are directed to:

- seek to understand why the taxpayer is in debt;
- emphasise the need for the taxpayer to take quick action to pay debts by using 'behavioural insights'; and
- arrive at a constructive solution that results in a greater likelihood of resolving the debt, such as requesting larger initial payments with next payment within a week.⁴⁴⁵

⁴⁴¹ *Legal Service Directions 2005*, app B.

⁴⁴² ATO, 'Service Delivery Plan', above n 168, p 15.

⁴⁴³ ATO, 'Debt Strategy 2014-18', above n 42.

⁴⁴⁴ ATO, 'Debt Engagement', above n 53.

⁴⁴⁵ *Ibid.*

- 4.175 The ATO has also advised during the review that it had finalised and begun training across the DBL on 'natural conversations' and negotiation skills, such as understanding the taxpayer and adapting negotiation strategy and communication style to secure payment based on the taxpayer's propensity to pay. All debt staff are expected to complete this training.⁴⁴⁶
- 4.176 The ATO's new debt strategy recognises that taxpayer engagement 'cannot happen without a conversation' and early engagement with taxpayers increases the likelihood of cases finalising. The ATO states that its engagement activities are designed to seek all reasonable opportunities to have that 'conversation'.⁴⁴⁷
- 4.177 Such strategies aim to address previously identified communication issues, for example, the earlier mentioned internal ATO reports on garnishees notices which found that staff may be attempting insufficient contact with taxpayers before taking firmer action.⁴⁴⁸
- 4.178 The ATO has also advised that it reviews taxpayer complaints to take proactive response to address the cause. For example, the issue of taxpayers being unaware of debts being treated as uneconomic to pursue and then subsequently being re-raised, was referred to the ATO's Design and Delivery unit for consideration. As a result, warning letters are now issued when 'bulk non-pursuits' are completed.⁴⁴⁹

IGT observations

- 4.179 As noted in Chapter 2, the ATO has recently started to develop a tailored debt engagement framework which should allow better differentiation of engagement with taxpayers. The IGT believes that this may result in more appropriate engagement strategies for different taxpayers.
- 4.180 The ATO is also attempting to achieve large scale organisational change in culture towards better engagement with taxpayers. The IGT recognises that such a change would be beneficial but may take some time to be achieved. In the meantime, there is still a need for ATO staff to be able to effectively communicate with taxpayers to persuade them to pay their tax voluntarily. Such skills are crucial, particularly where some taxpayers do not prioritise the payment of their taxes. The IGT observes that, recently, the ATO had developed training in this respect. Such training could enable staff to differentiate their communication and engagement with taxpayers.
- 4.181 Furthermore, better supervision, advice and precedents, as discussed earlier in this chapter, may address many of the issues in relation to ATO officer's engagement with taxpayers, such as attempting more frequent contact with taxpayers, disclosing payment assistance and responding to taxpayers' questions.

⁴⁴⁶ ATO, Communication to the IGT, 2 March 2015.

⁴⁴⁷ ATO, 'Roadshow', above n 173.

⁴⁴⁸ ATO, 'Garnishees and Complaints', above n 346; ATO, 'Garnishee Review', above n 347, p 6.

⁴⁴⁹ ATO, Communication to the IGT, 18 November 2014.

- 4.182 The ATO's procedures should also support frequent communication with both taxpayers and their advisers to ensure they are both aware of ATO correspondence. This would address concerns where tax advisers have not been aware of ATO correspondence.
- 4.183 Furthermore, ATO communications with taxpayers concerning their debts can have a significant impact on taxpayers' trust and perceptions of fairness. The ATO is aiming to improve debt management letters to address taxpayer understanding and expected actions as discussed in Chapter 2.

ACCURACY AND CURRENCY OF INFORMATION UNDERLYING DEBT RECOVERY

- 4.184 As identified in the earlier sections of this chapter, certain ATO debt recovery activities had commenced on the basis of inaccurate information, such as where tax liabilities had in fact been paid in full or pursuant to agreed payment arrangements as well as where PAYG Instalments had been correctly varied.
- 4.185 Another key inaccuracy appeared to be in relation to taxpayers' address data maintained by the ATO. Such inaccuracies had resulted in garnishee notices being issued, DPNs not being received or cases referred to EDCAs.
- 4.186 Other inaccuracies were also raised where incorrect bank accounts had been garnished, such as those held in a taxpayer's capacity as trustee.
- 4.187 The relevant ATO materials have been described in the earlier sections of this chapter as well as specific discussions. However, it is necessary to draw together the theme of inaccurate information.
- 4.188 The IGT has identified a need for the ATO to have in place sufficient processes in place to ensure the alignment of its payment and accounting systems with its case management systems. Furthermore, internal ATO reports have found that there are significant issues in relation to officers not properly updating or making adequate notes within its case management systems. The IGT believes that both issues could result in recovery action commencing on the basis of inaccurate information, such as where payment arrangements had been negotiated.
- 4.189 Internal ATO reports have also identified significant issues with respect to incorrect taxpayer addresses being used, such as inconsistencies in addresses used between different types of correspondence. To reassure itself that taxpayers have received correspondence, as already stated, the IGT considers that the ATO should require its officers to make every effort to attempt contact before taking firmer recovery action. However, it is acknowledged that for some correspondence, such as in relation to DPNs, it is important to rely on deemed service to taxpayers.

- 4.190 Lastly, in relation to incorrect accounts being garnished by the ATO, such as those which are held by taxpayers in their capacity as trustee, another internal ATO report found that such issues may arise either due to systems data matching errors, staff error or possibly a lack of procedural information for staff. To address these potential issues, the IGT has recommended that the ATO clarify its staff processes in this respect as well as allow financial institutions to challenge the garnishee notice where they believed the notice is in relation to an incorrect account.
- 4.191 More broadly, to ensure that ATO staff adhere to processes, such as attempting phone contact with taxpayers before taking firmer action, the IGT has recommended there was a need for better supervision of staff.

CHAPTER 5 – ATO USE OF EXTERNAL DEBT COLLECTION AGENCIES

5.1 As described in Chapter 1, the ATO engages a panel of EDCAs to assist with resolving lower value debt cases that would otherwise have received no further action.⁴⁵⁰ There are a range of stakeholder concerns in this regard.

SUMMARY OF STAKEHOLDER CONCERNS

5.2 Stakeholders' views and concerns with the ATO's use of EDCAs include:

- whether the ATO should use EDCAs as a matter of principle;
- the ATO should refer only the more egregious cases to EDCAs;
- EDCAs operate inflexibly and inconsistently with ATO guidelines and taxpayers may not engage with the ATO once debts are referred to EDCAs;
- debt recovery activities being referred to EDCAs where debts were paid completely or reduced as per agreed payment arrangements; and
- inappropriate EDCA conduct and methods of communicating with taxpayers and their representatives.

USE OF EDCAs AS A MATTER OF PRINCIPLE

5.3 Stakeholders had mixed views on whether, as a matter of principle, the ATO should use EDCAs to collect tax debts. Some stakeholders who supported their use considered tax debts to be no different to commercial debts and that EDCAs provide a flexible resourcing option for the ATO to recover debts. However, others were fundamentally opposed to the use of EDCAs as they believed that:

- EDCAs are not part of the ATO but a business which seeks to profit from tax debts which the ATO 'sells';
- the ATO can recover tax debts at a lower cost than EDCAs; and
- taxpayers' sensitive financial information, which the ATO provides to EDCAs, was not secure and may be misused.

⁴⁵⁰ The current panel of ATO EDCAs are: Baycorp Collection Services Pty Ltd; Dun and Bradstreet; Probe Group Pty Ltd; and Recoveries Corporation Group Limited.

ATO information

- 5.4 The ATO believes the use of EDCAs to recover tax debt, on its behalf, is in accordance with section 8(1) of the TAA 1953. Under this provision, the Commissioner has delegated to the Deputy Commissioner a wide range of powers, including those under Schedule 1 to the TAA 1953 which relates to the collection and recovery of taxes. Pursuant to these delegated powers, the Deputy Commissioner has authorised EDCA employees to exercise these powers on the ATO's behalf⁴⁵¹ and advises taxpayers of this in the 'privacy statement' contained in the relevant letter that is issued to them.⁴⁵²
- 5.5 The ATO also states that the tax law⁴⁵³ enables the Commissioner to disclose taxpayer information to third parties who have been appointed to carry out a duty or function under a tax law.⁴⁵⁴
- 5.6 Furthermore, the ATO has publicly stated that it does not 'sell' taxpayers' debt to EDCAs and any uncollected debt remains the ATO's responsibility to collect.⁴⁵⁵ In this respect, the ATO pays EDCAs on a 'per case' basis using progressive rates which depend upon the volume of cases actioned each financial year and the type of service rendered, for example, various communication (such as reminders), securing payment in full or by arrangement or undertaking tracing.⁴⁵⁶ Additionally, EDCAs do not receive payments of the debts they pursue. Any such payments are made through the ATO's existing payment channels.⁴⁵⁷
- 5.7 The ATO has also stated that it uses EDCAs to complement its debt management strategies and to support the optimisation of voluntary payments by freeing up the ATO's experienced debt recovery resources to focus on more difficult recovery cases. The ATO also asserts that the use of EDCAs increases the number of lower risk taxpayers contacted and provides more opportunities to re-engage for those who have not responded to previous demands for payment.⁴⁵⁸
- 5.8 The ANAO has reviewed the efficiency of the ATO's EDCA program and noted that, between October 2007 and 31 December 2011, the ATO had referred approximately 1.8 million debt cases to EDCAs valued at approximately \$7 billion. The EDCAs had prompted the payment of approximately \$2 billion (29.1 per cent) at a cost of \$54 million to the ATO.⁴⁵⁹ More recent ATO data was described in Chapter 1.⁴⁶⁰

451 ATO, *Referral of Debt to External Collection Agencies* (13 June 2013) <<https://www.ato.gov.au>>.

452 Ibid.

453 *Taxation Administration Act 1953* s 8WB(1A).

454 ATO, 'Referral to EDCAs', above n 451.

455 Ibid.

456 ATO, Communication to the IGT, 11 July 2014.

457 ATO, 'Referral to EDCAs', above n 451.

458 Ibid.

459 ANAO, *The Engagement of External Debt Collection Agencies*: Australian Taxation Office (2012) p 16.

460 ATO, Communication to the IGT, 11 July 2014.

- 5.9 At the time of the ANAO's report in mid-2012, the ATO did not assess the impact of the EDCA program with broader debt management measures, such as the reduction in the overall level of debt holdings and changes in taxpayers' compliance behaviour. For example, in the 2010-11 financial year, the level of total collectable debt had reduced by 4 per cent (from \$14.7 billion in 2009-10 to \$14.1 billion in 2010-11)⁴⁶¹ for which the ATO considered the EDCA program and other measures contributed, such as the ATO writing-off \$3.8 billion in debt for that year. However, the ATO did not quantify the EDCA's contribution to the overall reduction.⁴⁶² As a result, the ANAO recommended the ATO 'establish the relative costs of the use of [EDCAs] and the ATO's internal processes'⁴⁶³. It was also considered that such comparison would support better selection of debt cases for referral and the management of those that are unresolved by EDCA action.⁴⁶⁴ In this respect, the ATO has advised that it has since:
- conducted a study to track the collection outcomes on a sample of cases across the four contracted EDCAs and the EI approach;
 - tracked collection outcomes across a sample of case groups to establish the indicative value of the Pre-Referral Warning Letter (PRWL) within the EI approach;
 - conducted a cost per call analysis comparing EDCAs and the ATO's CS&S Outsource and Early Collections team processes; and
 - determined the cost for EDCAs to collect \$1,000 (which has reduced from \$9.13 in 2012-13 to \$7.64 in 2013-14).⁴⁶⁵
- 5.10 As a result of these analyses the ATO found that the relative costs of using EDCAs are generally on par or slightly below the ATO's internal cost.⁴⁶⁶
- 5.11 In relation to the information that the ATO provides to EDCAs, such information can be grouped into four categories:
- client data – mostly identifying information, such as personal information, case identifiers as well as any tax agent details;
 - contact data – taxpayer contact details;
 - address data – taxpayers' addresses; and
 - postings data – details of taxpayers' debts, such as dates debts were created and due as well as the composition of the debt, such as the primary amount, interest and penalties.

461 Commissioner of Taxation, Annual Report 2009-10 (2010) p 50; Commissioner of Taxation, Annual Report 2010-11 (2011) p 50.

462 ANAO, above n 259, p 18.

463 Ibid, p 27.

464 Ibid, p 17-18.

465 ATO, Communication to the IGT, 29 January 2015.

466 Ibid.

- 5.12 Although the ATO makes such information available to EDCAs, the EDCAs currently do not have access to ATO systems.⁴⁶⁷ Rather, EDCAs use their own systems to manage the cases which the ATO refers to them.⁴⁶⁸ However, the ATO is trialling the provision of an ATO terminal to EDCAs which is discussed in the later section on information accuracy.
- 5.13 In handling taxpayer information, EDCAs are required to meet the same Commonwealth privacy and security requirements which apply to the ATO, such as the *Privacy Act 1988* and section 16 of ITAA 1936, as they are performing a tax law function under authorisation by the ATO. The EDCA personnel are also subject to the same scrutiny as ATO employees, such as undergoing external police checks, and are also required to sign a secrecy declaration that sets out their responsibilities and obligations to safeguard information disclosed to them. The ATO also assures itself of the security of taxpayer information held by EDCAs through contractual terms which imposes obligations to protect this information at all times and only use it in relation to rendering services to the ATO. Before referring cases to EDCAs, the ATO also completes physical and technology security audits on each EDCA to ensure that all privacy and security requirements are in place.⁴⁶⁹
- 5.14 Additionally, EDCAs are open to scrutiny and audit processes from a number of the ATO's external scrutineers. For example, the ANAO found no known breaches in the security of taxpayers' data during their 2012 review.⁴⁷⁰ Notwithstanding this finding, the ANAO observed that, whilst the ATO had developed a data security framework, it lacked clearly defined roles and responsibilities of key ATO Information and Communication Technology (ICT), physical security and debt staff in implementing the requirements of the framework which reduced the assurance that taxpayers' data was being adequately protected. As a result, the ANAO recommended that the ATO:
- clearly defines the respective roles and responsibilities of the Debt business line and the Trusted Access branch and the Security Policy and Services branch; and
 - implements all elements of the security framework, particularly the scheduling of reviews, and the completion of Certificates of Assurance and other requirements as set out in the Deeds of Standing Offer with the [EDCAs].⁴⁷¹
- 5.15 In response to this recommendation the ATO has advised that it had developed an Information Security Framework which contains four key plans that together form a governance framework for information security management for EDCAs. These plans are:
- the Service Level Agreement (SLA) – defines roles and responsibilities for the three areas responsible for the ICT and physical security governance namely, ATO Trusted Access, Security Policy & Services and EDCA Management;

467 ATO, Communication to the IGT, 11 July 2014; ATO, 'Referral to EDCAs', above n 451.

468 ATO, 'Referral to EDCAs', above n 451.

469 ATO, External Collection Agencies (26 August 2013) <<https://www.ato.gov.au>>; ATO, Communication to the IGT, 11 July 2014.

470 ANAO, above n 259, p 16-17.

471 Ibid, p 26.

- an assurance activity schedule – includes the ‘role, responsibilities and delivery dates’;
- a Certificate of Assurance – requires evidence to support that key operational, ICT and physical security requirements have been met; and
- a Certificate of Assurance Measurement document – outlines how the ongoing review of evidence provided via the Certificate of Assurance will occur.⁴⁷²

IGT observations

- 5.16 Although the ATO may legally engage EDCAs to assist with the recovery of tax debts, stakeholders who oppose such engagement, do so on a number of grounds. Whilst these concerns are valid, the IGT believes they may be largely mitigated.
- 5.17 Before discussing these grounds it should be recognised that the ATO does not ‘sell’ tax debts to EDCAs as they are not paid by reference to the amount of debts recovered as is the case in some countries. For example, in the United Kingdom, EDCAs are ‘paid commission only on successful recoveries’,⁴⁷³ and in the United States, when EDCAs were engaged by the IRS, they were paid on the basis of ‘extracting the maximum amount with respect to a fixed liability’.⁴⁷⁴ The ATO’s agreements with EDCAs show that they are paid depending on the number of cases they action each year and the type of work performed.
- 5.18 However, due to the commercial nature of EDCAs there may be a misalignment in how they approach work to satisfy performance obligations compared to the ATO. For example, it has been alleged that EDCAs may pressure taxpayers, who are likely to be lower income taxpayers with less financial knowledge, into unaffordable payment arrangements which can adversely impact their welfare and ability to access payment assistance in future. Such an approach may be inconsistent with the values contained in the *Taxpayers’ Charter* and the conduct expected in the APS. Whilst EDCAs are required to adhere to these values as part of their contracts with the ATO, the requirements are only meaningful to the extent there are consequences for any breaches. This issue is related to, more broadly, taxpayer protections for which the IGT has announced a review as part of his 2014 work program.
- 5.19 It should be noted that the ATO’s data suggests that EDCAs prompt the recovery of a substantial proportion of collectable debt which the ATO has been unable to collect at a cost largely comparable to the cost that the ATO would have incurred if they carried out the same work. Additionally, the use of EDCAs provides the ATO with flexibility in resourcing.

⁴⁷² ATO, Communication to the IGT, 29 January 2015.

⁴⁷³ OECD, ‘Tax Debt Management’, above n 45, p 75.

⁴⁷⁴ National Taxpayer Advocate, ‘Letter to Congress’ above n 135, pp 3, 7.

- 5.20 On the other hand, it may be argued that the above efficiencies may be gained at the expense of undesired taxpayer experience, such as unsustainable payment arrangements, which may adversely impact long-term behaviours. However, these factors have not been verified or measured by the ATO.
- 5.21 Accordingly, it would be prudent for the ATO to measure all impacts of the use of EDCAs and share them with the public to either assuage their concerns or for a more informed debate to take place. The publication of such material should be transparent and useful for users but it is recognised that certain disclosures may need to take account of sensitive commercial information. The outsourcing of a given activity provides a useful benchmarking opportunity to assess service and performance delivery which is discussed later in this chapter.
- 5.22 The IGT believes that the ATO should also consider other options to more effectively engage with taxpayers at earlier points in time and further encourage longer term payment behaviour. Such an option involves the ATO working closer with tax agents and, for example, giving them some ability to discuss payment arrangements with their clients for low value, low risk cases. This option would enable more timely engagement with taxpayers on their tax debts and secure improved outcomes due to the infancy of the debt and contemporaneous involvement of a trusted adviser. Such an option may also benefit tax agents by providing them with an incentive for more responsive client engagement. However, this option could only be pursued if any potential conflicts of interest could be addressed through such means as setting out appropriate parameters within which tax agents could operate and retaining the right to dissolve any of their actions if strict guidelines were not observed.⁴⁷⁵
- 5.23 In relation to the security of taxpayer information, EDCAs must meet the same obligations as the ATO. The ATO has in place a system to periodically test EDCAs, as mentioned in the section above, and has taken action to implement the recommendations of the ANAO to improve its information security framework. As the ATO's physical and ICT security requirements of EDCAs have recently been reviewed, the IGT considers this area may be better examined after the resulting changes have had time to be implemented.
- 5.24 However, the IGT believes that the ATO could assuage many stakeholder concerns in relation to the security of information, if TFN information was not provided to EDCAs unless it is absolutely necessary to perform their function. In these cases, the IGT believes that EDCAs could seek specific information from the ATO with TFNs being made available to them in exceptional cases.

⁴⁷⁵ ATO, *Letter to the editor of The Sydney Morning Herald and The Age* (2014) <<https://www.ato.gov.au>>.

RECOMMENDATION 5.1

The IGT recommends that the ATO measure and publish information relating to the performance of External Debt Collection Agencies, including the use of benchmarking, on aspects such as the:

- (a) efficiency of the pursuit of collectable debt;*
- (b) sustainability of payment arrangements; and*
- (c) impact on taxpayers and their long-term payment compliance behaviour.*

ATO response: Agree In Principle

The ATO commits to providing a more comprehensive view of the effectiveness of the ATO's debt management strategies, including those using our External Debt Collection Agency (EDCA) partners, in future annual reports. The information will be published at an external partners' strategy level, with no reference to individual agency results.

The amount of information that we can publish relating to the performance of EDCAs is impacted by the commercially sensitive nature of our contracts with those agencies.

REFERRAL TO EDCAs

- 5.25 Stakeholders generally expect the ATO to refer more egregious cases to EDCAs for recovery rather than lower value and lower risk cases. Stakeholders have said that the misalignment in expectations can result in future non-compliance as taxpayers believe they are being treated too harshly.
- 5.26 Stakeholders have also said that an uncertain volume of referred cases creates an inability for EDCAs to effectively plan for resourcing which can adversely impact their ability to collect tax debts in a timely manner.

ATO materials

- 5.27 The ATO has stated on its website that it only refers to EDCAs those debts that are 'low value' and 'non-complex'.⁴⁷⁶
- 5.28 Furthermore, the debt cases, which the ATO refers to EDCAs, are contractually defined and include:
 - income tax and activity statement debts;
 - superannuation guarantee debts; and
 - other debts owed to the Commonwealth.⁴⁷⁷

⁴⁷⁶ ATO, *Debt Collection – What to Expect* (20 May 2014) <<https://www.ato.gov.au>>.

5.29 The above debts must also be:

- in relation to ‘active cases’ which are not affected by the taxpayer’s ability or requirement to resolve the debt, such as taxpayers with disputed debts or who are insolvent or deceased/deregistered; and
- ‘within the potential project and dollar ranges for external referral’.⁴⁷⁸

5.30 The system processes for referral to EDCAs were described in Chapter 1.⁴⁷⁹ Additionally, the ATO sends PRWLs at least 14 days before the cases are referred to EDCAs to give taxpayers another opportunity to contact the ATO.⁴⁸⁰ If taxpayers do not respond to the letter within a specified time, or if the taxpayer has had a warning letter issued previously, the case may be referred.⁴⁸¹ It should be noted that some taxpayers may not receive a PRWL at all if they have previously had a case referred to EDCAs before PRWLs were developed.⁴⁸²

5.31 In relation to the number of cases referred to EDCAs, the ANAO had observed that this varies as a result of the fluctuating nature of ATO funding and that the ATO had not determined an allocation method for sharing work across its panel of EDCAs.⁴⁸³

5.32 The ATO, however, has advised that EDCAs are provided a referral forecast on a quarterly basis. Furthermore, the ATO’s EDCA Management unit has recently developed a Performance Base Referral (PBR) allocation model that determines referral numbers and is reviewed on a monthly basis. The PBR is divided into two defined metrics:

- financial metric comparison — based on a 3, 6 and 12 month ‘rolling recovery rate’ which is intended to provide the ATO with assurance that the EDCAs are effectively managing case referrals in the short, medium and long term; and
- non-financial (contractual obligations) — focused on ‘delivery, customer satisfaction and relationship’.⁴⁸⁴

5.33 The tables below show the ATO’s relative distribution of work to its different EDCAs.

Table 5.1: Distribution of work to EDCAs from July 2012 to December 2014

Years	Probe	Recoveries	Dun & Bradstreet	Baycorp	Totals
2014–15	80,002	55,104	63,265	48,680	247,051
2013–14	176,856	114,112	127,847	95,693	514,508
2012–13	118,356	151,291	173,214	95,519	538,380

Source: ATO.

⁴⁷⁷ ATO, Communication to the IGT, 11 July 2014.

⁴⁷⁸ Ibid.

⁴⁷⁹ Ibid.

⁴⁸⁰ ATO, ‘Debt Collection – What to Expect’, above n 476.

⁴⁸¹ ATO, Communication to the IGT, 11 July 2014.

⁴⁸² Ibid; ATO, Communication to the IGT, 29 January 2015.

⁴⁸³ ANAO, above n 259, p 21.

⁴⁸⁴ ATO, Communication to the IGT, 29 January 2015.

Table 5.2: Distribution of work to EDCAs over 2010–11 to 2011–12

Years	National Credit Management Ltd (NCML)	Recoveries	Dun & Bradstreet	Baycorp	Totals
2011–12	10,667	110,089	100,055	79,209	300,020
2010–11	104,033	104,946	101,786	103,447	414,212

Source: ATO.

- 5.34 The tables above show that there can be a large variation in the number of cases that are referred to different EDCAs.

IGT observations

- 5.35 At a strategic level, the ATO needs to ensure that the EDCA program is integrated with its broader approach to debt management to ensure that the ATO takes the most effective action in the first instance for every case.
- 5.36 The ATO's work to identify 'next best treatments', discussed in Chapter 2, should allow the ATO to identify those cases that are more likely to respond to an EDCA.⁴⁸⁵ This work could then improve the effectiveness of EDCA referrals as a treatment strategy.
- 5.37 However, whilst the ATO has a debt referral process to ensure the consistency of selecting and referring debt cases to EDCAs, stakeholders expect different types of cases to be referred despite the ATO's public statements.⁴⁸⁶ The ATO, however, does not publish a comprehensive description of the referral process. The IGT believes that a more detailed disclosure of the referral process to EDCAs may help to realign community expectations and, therefore, mitigate any perverse taxpayer behaviours which may result due to misconceptions.
- 5.38 Furthermore, whilst the ATO's contracts (Deeds of Standing Offer or DOSO) with its EDCAs provide the ATO with flexibility in relation to the volume of cases it refers to EDCAs, the IGT considers that sufficient warning should be given of changes and unexpected increases in numbers of case referrals to EDCAs. This would better allow EDCAs to effectively plan their resourcing to meet their performance obligations. Accordingly, the current quarterly estimates of the volume of cases to be referred, should be made and provided to EDCAs more frequently, such as on a monthly basis.

RECOMMENDATION 5.2

The IGT recommends the ATO:

- (a) *publish the types of debt collection work for which it engages External Debt Collection Agencies and the types of cases referred to them; and*
- (b) *provide External Debt Collection Agencies with more frequent estimates of the volume of cases to be referred so that they can better manage resources and meet performance obligations.*

⁴⁸⁵ ANAO, above n 259, p 17-18.

⁴⁸⁶ ATO, 'Debt Collection – What to Expect', above n 476; ATO, 'Referral to EDCAs', above n 451.

ATO response: Agree

The ATO advises these matters will be negotiated in future commercial in-confidence contracts between the ATO and individual EDCA partners.

OVERSIGHT AND SCOPE OF AUTHORITY OF EDCAs

5.39 Stakeholders question how the ATO ensures EDCAs act in accordance with the required guidelines as they have observed that some EDCAs:

- have been inflexible and inconsistent in their approach to collecting tax debts; and
- do not appear to have authority to enter into payment arrangements, remit interest or negotiate disputed debts, whilst other EDCAs can do so to a limited extent.

5.40 Stakeholders also raised concerns that taxpayers cannot speak with the ATO once debts are referred to EDCAs as such a requirement creates unnecessary additional work.

ATO materials

5.41 The ATO's EDCAs are required to provide debt collection services in accordance with the:

- Australian Competition and Consumer Commission and ASIC *Debt Collection Guideline for Collectors and Creditors*;
- terms of the DOSO with the ATO;
- APS Code of Conduct within the *Public Service Act 1999*;
- ATO Ethical Business Relationships Statement; and
- ATO collection guidelines (including debtor contact/proof of identify, *Taxpayers' Charter*, *Compliance Model* and Privacy, Complaints Procedures, Collection Instructions, Payment Guidelines and Authorisations).⁴⁸⁷

5.42 In providing collection services, the ATO has authorised EDCAs to, amongst other things:

- secure payment in full;
- enter into payment arrangements for liabilities which are no greater than \$500,000 and do not exceed a term of 36 months;
- remit GIC amounts no greater than \$25,000; and
- refer certain cases back to the ATO for action.⁴⁸⁸

⁴⁸⁷ ATO, Communication to the IGT, 11 July 2014; ATO, 'Referral to EDCAs', above n 451.

- 5.43 When initially contacting taxpayers, the ATO's collection guidelines state that EDCAs must request payment in full and obtain details of how payment will be made.⁴⁸⁹ However, these guidelines acknowledge that there may be circumstances which prevent a taxpayer from paying their debt in full. In such cases, EDCAs are to attempt to gain an upfront payment and negotiate payment of the remaining debt over the shortest possible timeframe taking into account the taxpayer's personal circumstances. The ATO also requires EDCAs to make payment arrangement decisions in accordance with Practice Statement PS LA 2011/14. In limited situations, EDCAs may also, with the ATO's approval, enter into interest free arrangements with small business taxpayers.⁴⁹⁰
- 5.44 The ATO believes that the authority granted to EDCAs to enter payment arrangements should cover the majority of cases referred to them. Where EDCAs cannot negotiate a payment arrangement due to authorisation limitations, the cases will be referred back to the ATO for action.⁴⁹¹
- 5.45 EDCAs are also not required to accept taxpayers' payment proposals as matter of course and are authorised by the ATO to refuse payment arrangements. In doing so, EDCAs will provide reasons verbally for their decisions as well as advise the taxpayer of their rights of review.⁴⁹²
- 5.46 In relation to remitting GIC, where a taxpayer has requested remission, EDCAs are to:
- assess the taxpayer's financial situation;
 - identify the reasons which contributed to the non or late payment of liabilities; and
 - ensure that all lodgments are up to date.⁴⁹³

488 ATO, 'Instrument of Authorisation: Dun & Bradstreet (Australia)' (Internal ATO document, 2014); ATO, 'Instrument of Authorisation: Recoveries Corporation' (Internal ATO document, 2014); ATO, 'Instrument of Authorisation: Probe Group (Australia)' (Internal ATO document, 2014); ATO, 'Debt Collection Services: Collection guidelines for external collection agencies working on behalf of the ATO in line with their Deed of Standing Offer' (Internal ATO document, 2013) p 27.

489 ATO, 'Guidelines for EDCAs', above n 488, p28; ATO, 'Referral to EDCAs', above n 451.

490 ATO, 'Guidelines for EDCAs', above n 488, p28, 32; ATO, 'Referral to EDCAs', above n 451.

491 ATO, 'Guidelines for EDCAs', above n 488, p28, 32.

492 Ibid, p 34; ATO, 'Referral to EDCAs', above n 451.

493 ATO, 'Guidelines for EDCAs', above n 488, pp 38-39.

- 5.47 The EDCAs must then contact the ATO to ascertain the taxpayer's compliance history and the total amount of GIC to be remitted. For low risk cases, where GIC is not more than \$2,500, EDCAs may immediately remit the GIC if the taxpayer has a good compliance history or may consider whether remission would be appropriate under PS LA 2011/12 if the taxpayer does not have a good compliance history. Where GIC is between \$2,500 and \$10,000, EDCAs must consider whether remission is appropriate pursuant to PS LA 2011/12 regardless of a taxpayer's compliance history. In making these decisions, the ATO has stated that EDCAs are required to follow the same guidelines as its own staff.⁴⁹⁴
- 5.48 Cases involving the remission of GIC amounts greater than \$10,000 must be referred to the ATO for a decision.⁴⁹⁵
- 5.49 Where a taxpayer's debt is disputed, EDCAs are directed to establish the amount which the taxpayer is disputing. If the taxpayer is disputing the full amount, the EDCA must advise the taxpayer to contact the ATO and then cease action on the case for 30 days to allow the taxpayer time to lodge their dispute. Once a dispute is received by the ATO, taxpayers will then receive a formal notification from the ATO and the case will be withdrawn from the EDCA.⁴⁹⁶ If no dispute has been lodged, EDCAs are directed to continue with their collection activity.⁴⁹⁷
- 5.50 If the taxpayer is only disputing part of their debt, EDCAs are directed to attempt to collect the undisputed amount.⁴⁹⁸
- 5.51 A dedicated email address has been established by the ATO for EDCAs to refer cases to the ATO for action, advice or information. If matters are urgent, EDCAs may also phone the ATO. However, the ATO expects EDCAs to resolve issues internally where possible before escalating the matter.⁴⁹⁹ The ATO also expects that once a case is referred to an EDCA, it remains under their management and they are responsible for the collection and monitoring of the debt until it is withdrawn by the ATO. Furthermore, where the ATO receives calls in relation to referred cases, ATO staff are instructed to transfer taxpayers' calls to the relevant EDCA.⁵⁰⁰
- 5.52 To help ensure that EDCAs are adhering to the above expectations, the ATO has in place SLAs, with its EDCAs, which sets out a 'performance management framework', including performance measures and minimum expected standards. The SLAs also establish a formal process to regularly assess and review EDCA performance as well as to identify, document and resolve potential and emerging issues that may inhibit EDCA performance.⁵⁰¹ Some of the key measures and associated reporting requirements outlined in the SLAs are described below:
- certificate of assurance — includes an 'Exception report' for all unmet controls;

494 ATO, 'Referral to EDCAs', above n 451.

495 ATO, 'Guidelines for EDCAs', above n 488, pp 38-39, apps L, M O; ATO, 'Referral to EDCAs', above n 451.

496 ATO, 'Guidelines for EDCAs', above n 488, p 46.

497 Ibid.

498 Ibid.

499 Ibid, pp 56-57.

500 Ibid, pp 57-58; ATO, 'Referral to EDCAs', above n 451.

501 ATO, 'Service Level Agreement (SLA): For the provision of debt collection services to the Australian Taxation Office' (ATO) (Internal ATO document, 2013) p 3.

- collection performance – assesses EDCAs performance in line with the minimum standards as well as benchmarking;
 - debt case action – sets key benchmarks for referred cases, such as requiring 100 per cent of all cases to be actioned in accordance with the DOSOs and 45 per cent of all payment arrangements entered into by EDCAs to not be defaulted;
 - incident and complaint management – requires EDCAs to maintain an ‘issues register’ to record progress of all issues and problems, including service problems and complaints that arise and provide that register to the ATO; and
 - quality standards – states that the ATO may conduct ‘floor walking’ at the EDCA’s premises as well as review quarterly a sample of 30 referred debt cases, which are selected by EDCAs themselves, to assess performance in relation to the guidelines for which the ATO sets a 95 per cent benchmark.⁵⁰²
- 5.53 Additionally, EDCAs are required to actively and accurately monitor, measure and record other performance indicators that would reasonably assist the ATO in benchmarking, improving processes or measuring the level of value delivered by EDCAs amongst other things.⁵⁰³
- 5.54 Where an EDCA is failing to achieve a required minimum performance standard, the EDCA is required to document and report the default to the ATO, investigate the issue and take remedial action to prevent it from reoccurring.⁵⁰⁴ The ATO also has in place a ‘service rebate and credit scheme’. Under this scheme, the ATO may, in its discretion and depending on the severity of any default, deduct amounts otherwise payable to EDCAs. However, EDCAs are able to regain any deducted amount by implementing remedies within a timeframe agreed with the ATO.⁵⁰⁵
- 5.55 It should be noted that the above scheme does not inhibit any other rights that the ATO may have under its contracts with the EDCAs.⁵⁰⁶

IGT observations

- 5.56 As stakeholders are concerned with the ATO’s use of EDCAs generally, it is important that taxpayers are made fully aware of the scope of EDCA authority so that expectations are appropriately managed. Whilst the ATO’s internal documents set out the activities that EDCAs may undertake, including where matters should be referred to the ATO, it appears that such information is not made publicly available. The IGT believes that better appreciation of EDCA’s authority and the ATO’s collection guidelines would clarify, for stakeholders, the limited actions that EDCAs may take in relation to payment arrangements, remission of interest and disputed debts.

⁵⁰² Ibid, pp 5-10; ATO, Communication to the IGT, 29 January 2015.

⁵⁰³ ATO, ‘EDCA SLA’, above n 501, p 14.

⁵⁰⁴ Ibid.

⁵⁰⁵ Ibid, pp 14-15.

⁵⁰⁶ Ibid pp 15.

- 5.57 It follows that those cases which are referred to EDCAs for resolution should be within their authority to resolve. For example, if it is expected that a taxpayer may require a payment arrangement which is beyond the authority of EDCAs, such cases should not be referred, but rather managed by the ATO itself. Whilst the ATO expects the majority of cases referred to be within the EDCA's authority to resolve, an inability to resolve cases may frustrate taxpayers and contribute to an inefficient process. The IGT notes that there is also a discrepancy between the ATO's guidelines to EDCAs (as well as public statements) and EDCA authorisations which provide that they can remit interest up to \$10,000 and \$25,000 respectively.⁵⁰⁷ Accordingly, the IGT believes that the ATO should better align its referral criteria with the authority granted to EDCAs.
- 5.58 Where a case is referred to an EDCA and it subsequently becomes apparent that resolution is outside the scope of the EDCA's authority, the system relies on the discretion of EDCAs to escalate the matter to the ATO. However, if an EDCA does not refer the matter and persists with its course of action, a taxpayer may become unsatisfied. In these circumstances, the ATO expects EDCAs to resolve complaints at first instance and only escalate those where resolution was not successful. It is only where complaints remain unresolved that EDCAs must disclose to taxpayers their right to lodge a formal complaint directly with the ATO.⁵⁰⁸ The IGT is of the view that delaying the disclosure of this right risks unnecessary escalation of taxpayer resistance and risks their disengagement from recovery processes.
- 5.59 The IGT considers that this risk could be avoided by disclosing at the outset, the taxpayers' rights to complain, however, that the ATO expects taxpayers to engage EDCAs to resolve their debt in the first instance. This information could form part of the letter which informs taxpayers that their debt has been referred to an EDCA. The IGT also observes that, as the ATO captures complaints made to EDCAs, this could be a source of valuable feedback to assess performance and maintain oversight of its EDCAs.
- 5.60 Maintaining sufficient oversight of EDCAs is required to provide assurance to the ATO that its expectations are being met. In addition to the complaints system above, the ATO's collection guidelines provides oversight of EDCAs by requiring ATO input into certain decisions made by EDCAs as well as other decisions which first require ATO authorisation before they may be made. The guidelines also provide a system for EDCAs to seek advice or escalate certain matters to the ATO. Limiting ATO involvement to more serious issues appears appropriate, otherwise it would assume the role for which EDCAs have been contracted.

⁵⁰⁷ ATO, 'Guidelines for EDCAs', above n 488, pp 38-39, Appendices L, M O; ATO, 'Referral to EDCAs', above n 451; ATO, 'D&B Authorisation', above n 488; ATO, 'Recoveries Corporation Authorisation', above n 488; ATO, 'Probe Group Authorisation', above n 488.

⁵⁰⁸ ATO, 'Guidelines for EDCAs', above n 488, p 53.

- 5.61 EDCA performance on meeting the ATO's expectations is measured and reported pursuant to the SLA, such as conducting reviews of a sample of referred debt cases totalling 120 annually. In the IGT's view, reviewing 120 cases in a high-volume area (up to 176,000 cases), which are selected by the EDCAs themselves, may be insufficient to ensure expectations are being met as well as ensuring consistency. Even in circumstances where it is considered not feasible to conduct a review of a larger random sample, there may be scope to conduct more targeted reviews of certain cases. For example, such reviews could be conducted in relation to cases which have generated common complaints as well as in relation to the key performance measures, such as cases where payment arrangements were defaulted. The IGT also recognises that monitoring the consistency of EDCA decisions comes at a cost to the ATO. Accordingly, limited monitoring could be accompanied by a more cost effective approach of ensuring EDCA personnel receive relevant and periodical training in relation to the ATO's specific expectations.
- 5.62 Furthermore, whilst contractual performance measures define the paramount objectives and behaviours expected of contractors, the IGT is concerned that two of the ATO's performance measures, 'collection performance' and 'debt case action', may encourage EDCAs to focus on recovering debts with less regard for taxpayers' circumstances or the sustainability of payment arrangements despite guidance to do so. This is because the ATO requires EDCAs to enter into payment arrangements with 'kept rates' of only 45 per cent (not defaulted). It is also uncertain how EDCAs determine the affordability of payment arrangements or whether they use the ATO's BVAT and DST in setting the parameters of payment arrangements. Accordingly, the IGT believes that the performance measures for EDCAs should include more consideration of the impact on taxpayers, providing them, for example with the streamlined BVAT recommended earlier in the report, DST or similar tools to consider taxpayers' circumstances.

RECOMMENDATION 5.3

The IGT recommends the ATO:

- (a) better inform the public about External Debt Collection Agencies' role particularly in relation to how they are required to act with respect to disputed debts, enter into payment arrangements and remit interest;*
- (b) increase taxpayer awareness on how they can make complaints about the actions of External Debt Collection Agencies from the outset; and*
- (c) assist External Debt Collection Agencies to give more consideration to taxpayers' circumstances.*

ATO response: Agree in Principle

As part of our communication and collaboration program we will continue to raise awareness of our strategies to collect debt including the use of our external partners.

We agree with the intent of (b) and note this will be covered in our broad communication and collaboration program.

We will continue to work in partnership with the External Debt Collection Agencies (EDCAs) to ensure consistency of approach for taxpayers regardless of whether they are interacting with the ATO or an EDCA.

ACCURACY OF INFORMATION PROVIDED TO EDCAs

- 5.63 Concerns in relation to the accuracy of information relied upon by the ATO when it undertakes debt recovery activities were discussed in Chapter 4. This section focuses on the accuracy of information provided by the ATO to EDCAs on referred debts.
- 5.64 Many stakeholders have observed instances which suggest that the ATO has given EDCAs inaccurate information, such as recovery activity commencing where debts have been paid completely, reduced as agreed under payment arrangements, before debts were due and where refunds were due.
- 5.65 Stakeholders have also made general observations that letters are sent to tax agents who no longer represent the taxpayer, EDCAs not knowing the debtor reference number quoted to them when taxpayers return their calls and issuing letters with names missing. Stakeholders have said these issues result in extra costs and time in trying to determine why such correspondence was sent.
- 5.66 Some stakeholders, however, have commented that information accuracy issues are currently mitigated by EDCAs communicating with the ATO's Debt Support Recovery Team (DSRT) to clarify information where necessary. These stakeholders believe that whilst such channels may be effective, they are inefficient. They have suggested that there needs to be investment in automation of the data interface between the ATO and EDCAs to provide updated information more frequently.

ATO materials

- 5.67 While a referred case remains active with an EDCA, the ATO's Operations Sub-plan Enterprise Reporting Team extracts relevant case data from the ATO's systems and transmits any information to be updated to EDCAs via the Corporate Exchange Gateway.⁵⁰⁹ Chapter 1 described this weekly transmission process.⁵¹⁰ It includes:
- cases referred (or re-referred) to EDCAs;
 - updated information for cases currently referred, including changes to addresses, contacts and debt values; and
 - details of cases that have become ineligible for referral and have been retrieved by the ATO.⁵¹¹

⁵⁰⁹ ATO, 'The Debt Referral Process', above n 141, pp 4, 9; ATO, ATO, 'Referral to EDCAs', above n 451.

⁵¹⁰ ATO, 'The Debt Referral Process', above n 141, pp 4, 9.

⁵¹¹ Ibid, p 9.

- 5.68 The ATO has stated that due to its current system limitations, a more frequent transfer of information is not possible.⁵¹² Therefore, to accommodate any changes to information which occur during the week, EDCA demand letters advise taxpayers to ignore the demand if payment had been made within the last seven days.⁵¹³ Additionally, where taxpayers call EDCAs with respect to having made payments, EDCAs are required to phone the ATO to confirm the payment. If the payment is not recorded as being received, the EDCA will place a hold on the case and check with the ATO again after one week to allow for any processing delays.⁵¹⁴
- 5.69 As indicated earlier, the ATO is currently trialling providing EDCAs with an ATO terminal to enable access to updated information in real-time which is expected to alleviate many of the concerns with the accuracy of information. The ATO has advised that the impetus for this trial was that EDCAs make a large number of calls to the ATO which are primarily to confirm taxpayer account balances (for example, during the 2013–14 financial year, EDCAs made 48,000 calls to the ATO's DSRT, of which, approximately 90 per cent were to check taxpayer account balances). To support this project, the ATO has developed a Fraud & Corruption Risk assessment plan which, amongst other things, includes random checks of physical security, additional training for EDCA staff as well as limiting access to information (including read only access) and internet connectivity.⁵¹⁵

IGT observations

- 5.70 It is important that EDCAs take action based on accurate and complete information to ensure that recovery activity is efficient and that taxpayers and their advisers are not subjected to unnecessary costs. When outdated information is used by EDCAs it may also reduce taxpayers' confidence in the authenticity of the EDCA and the expected standard of service.⁵¹⁶
- 5.71 Although, the ATO has a weekly process to update the information provided to EDCAs, there remains a margin for action to be taken on outdated information.
- 5.72 Ideally, real-time updates would reduce the risk of EDCAs actioning cases based on outdated information. However, such updates are currently not possible due to system limitations. As an alternative, the ATO is considering providing EDCAs with access to an ATO terminal. Whilst, such access will provide EDCAs with real-time access to ATO information, it may also create perceptions of inappropriate private sector access to sensitive taxpayer information. The IGT believes that if appropriate security safeguards are taken to reduce the risk of inappropriate access, the provision of an ATO terminal may be a feasible option to help reduce instances of recovery action taken on the basis of inaccurate information. Accordingly, the IGT believes that the ATO's Fraud & Corruption Risk assessment plan may be appropriate.

⁵¹² ATO, 'Referral to EDCAs', above n 451.

⁵¹³ Ibid.

⁵¹⁴ Ibid.

⁵¹⁵ ATO, Communication to the IGT, 29 January 2015.

⁵¹⁶ ANAO, above n 259, p 21-22, 91.

- 5.73 The ATO also has a responsibility to ensure that EDCAs maintain the accuracy of information provided to them as well as the information that EDCAs provide to taxpayers or their advisers, such as debt reference numbers. However, it appears that the ATO does not have such requirements of EDCAs nor are requirements outlined in the collection guidelines for EDCAs. The IGT believes that such requirements are necessary to ensure that EDCAs appropriately manage their own internal systems with regards to the accuracy of information.

EDCA COMMUNICATION

- 5.74 Stakeholders consider that some of the methods used by EDCAs to communicate with taxpayers and their representatives are inappropriate, such as using automated phone diallers and sending text messages which ask the recipient to call them. Stakeholders have also noted that tax agents are often contacted outside of standard business hours and some of their clients are being contacted directly. Furthermore, stakeholders have said that they need proof that EDCAs are acting on behalf of the ATO.
- 5.75 Submissions indicated that some taxpayers have refused to communicate with EDCAs because they have not given authority to the ATO to give their information to EDCAs. Similarly, some tax agents have also refused to communicate with EDCAs as they have not been given authority by their clients to do so.
- 5.76 Stakeholders have also raised a number of concerns with the effectiveness of EDCAs' communication during recovery activities, including:
- not providing sufficient information in voice messages for recipients to return phone calls who must then wait for the EDCA to call again;
 - attempting to pass themselves off as being from the ATO and wielding ATO powers; and
 - being aggressive, rude and abrupt in conversations with tax agents and taxpayers, for example, in one case despite a taxpayer agreeing to a payment arrangement with the EDCA, it charged the full amount of the debt to the taxpayer's credit card and threatened them when they called about the error.

ATO materials

- 5.77 As part of the ATO's DOSOs with EDCAs, it expects EDCA negotiations with taxpayers to be of the highest quality⁵¹⁷ and, as mentioned earlier in this chapter, pursuant to the APS Code of Conduct, *Taxpayers' Charter* and the ATO's debt collection guidelines, amongst other things. The ATO also has in place a complaints system in relation to its EDCAs.⁵¹⁸

517 ATO, 'External Collection Agencies', above n 469.

518 ATO, 'Referral to EDCAs', above n 451; ATO, Communication to the IGT, 11 July 2014.

- 5.78 EDCAs use a range of methods to collect debt, including initial contact by letter, followed by subsequent telephone and additional letter contact.⁵¹⁹ The ATO's guidelines are silent on the use of automated phone diallers but they do state that SMS may be used where approval has been granted by the ATO.⁵²⁰
- 5.79 The ATO has stated that whilst the EDCA's contracts allow for weekday and weekend contact, they currently only operate on weekdays. The use of after-hours contact (until 9.00pm on weeknights) by EDCAs is also consistent with the ATO debt collection practices. After hours contact is said to enable increased coverage of taxpayers as well as better contact with small business owners and operators who are generally busy during the day.⁵²¹
- 5.80 In making calls after hours, EDCAs specifically exclude identified tax agent phone numbers, who should only be called between 9:00AM and 5:00PM unless otherwise stated by the tax agent. The ATO accepts there may be some instances where a tax agent number is not identified and is called after hours in error.⁵²²
- 5.81 The ATO directs EDCAs to contact taxpayers' tax agents in the first instance, where such information is registered, to first determine if they are still representing the taxpayer.⁵²³ EDCAs may only call taxpayers or other authorised contacts directly where the tax agent either:
- does not return calls within a reasonable timeframe;
 - does not respond within the agreed timeframe;
 - advises the EDCA to speak directly with the taxpayer or authorised contact; or
 - advises the EDCA that they no longer represent the taxpayer.⁵²⁴
- 5.82 In making contact by phone, EDCA staff are required to identify themselves and their agency. They have also been provided with appropriate scripting to address concerns of taxpayers and tax agents about debts being referred to an external collection agency.⁵²⁵

IGT observations

- 5.83 The ATO allows EDCAs to use a variety of communication channels to improve contact with taxpayers and their advisers, including SMS messages.

519 ATO, 'Referral to EDCAs', above n 451.

520 ATO, 'Guidelines for EDCAs', above n 488, p 25.

521 ATO, 'Referral to EDCAs', above n 451.

522 ATO, 'Guidelines for EDCAs', above n 488, p 19.

523 Ibid.

524 Ibid.

525 ATO, 'Referral to EDCAs', above n 451.

- 5.84 Such communication is used after PRWLs have been sent to taxpayers or their agents. The IGT acknowledges that not all taxpayers may prefer the same forms of communication or be available to talk during business hours. However, the use of automated diallers and SMS once the initial letters have been sent are a less intrusive means by which to attempt contact with taxpayers as well as being a quick and cheap way to prompt taxpayers to call when they have time.
- 5.85 Furthermore, the ATO's guidelines do not permit EDCAs to contact tax agents outside of standard business hours unless advised by tax agents otherwise. The ATO acknowledges that such contact may occur in error where phone number data does not indicate the contact number is for a tax agent. The IGT believes that the current ATO guidelines, which allow tax agents to request EDCAs to call them during business hours, is sufficient. Where it is found that there are errors in phone number data, it should be properly referred to the ATO to update their systems. The IGT notes that the ATO has guidelines to make such updates.⁵²⁶
- 5.86 The ATO's guidelines for EDCAs also generally do not permit EDCAs to contact taxpayers directly but for certain limited situations. Such contact is uncontroversial where EDCAs are directed by the tax agent to call the taxpayer directly or where they no longer act for the taxpayer. However, the issue is where EDCAs contact taxpayers directly due to tax agents not responding. The IGT believes that sufficient latitude is afforded in the ATO's guidelines to allow tax agents to engage with EDCAs and it may be appropriate that the taxpayer is contacted directly to avoid any potential escalation to firmer debt recovery action, particularly where it may be through no fault of the taxpayer. As mentioned above, where such contact is made in error, EDCAs should update information as per the ATO's guidelines and taxpayers should be permitted to refer the call to their tax agent should they wish.
- 5.87 In relation to providing assurance that EDCAs are acting on the ATO's behalf, the ATO has in place two methods. One is a list on its website disclosing the panel of EDCAs and the other is a mechanism for taxpayers or the advisers to call back EDCAs using their main phone number which is disclosed on the ATO's website.⁵²⁷ The IGT believes these mechanisms may assuage concerns as to whether EDCAs are acting on behalf of the ATO. However, the IGT observes that details of the specific EDCA to which a taxpayer's debt is referred is not disclosed in any letter sent by the ATO to taxpayers. Accordingly, the IGT believes that including such information as well as reference and contact numbers for the specific EDCA may also help alleviate stakeholders' concerns about the authenticity of EDCAs.

⁵²⁶ ATO, 'Guidelines for EDCAs', above n 488, pp 20-21.

⁵²⁷ Ibid, pp 22, 47.

- 5.88 In relation to EDCA staff behaviour, they are required to be professional in their conduct and the DOSOs provides for a complaints system. The ATO accepts that complaints serve as important feedback and help it to identify improvement opportunities and specifically directs EDCAs to recognise a person's right to complain.⁵²⁸ As mentioned earlier, the ATO expects EDCAs to take all reasonable steps to resolve complaints within ATO policy but also to inform taxpayers of their right to make a formal complaint directly to the ATO. The ATO also monitors EDCAs incident and complaint management, amongst other things, and for which the 'service rebate and credit scheme' operates. The IGT believes this scheme may be sufficient if it effectively encourages EDCAs to address particular complaints.

⁵²⁸ Ibid.

APPENDIX 1: TERMS OF REFERENCE AND SUBMISSION GUIDELINES

BACKGROUND

The Australian Taxation Office (ATO) manages the revenue systems that sustain social and economic policy and funds services for Australians.⁵²⁹ The efficacy with which the ATO collects tax debts may impact upon government policy and services for Australians. Therefore, it is important for the ATO to consider the broad economic impact in doing so, however, the relevant taxpayers' circumstances should also be taken into account.

Over the last ten years, the ATO has reported an upward trend in total collectable debt,⁵³⁰ with more recent increases being attributed to economic conditions and the ATO assisting viable businesses to stay afloat. In 2012–13, the total amount of this debt was reported as \$17.7 billion, with 17.8 per cent of this amount outstanding for more than two years and over 60 per cent owed by small businesses.⁵³¹

During this period, the ATO has managed tax debts using a number of strategies, including initiatives aimed at improved contact with taxpayers, implementing a Business Viability Assessment Tool (BVAT) as well as using external debt collection agencies (EDCAs) to recover lower-value, non-complex debts. The ATO may take a range of actions to recover debts, from simply requesting payment to firmer actions such as garnishee notices and insolvency proceedings. The ATO may also assist taxpayers to pay their debts through such means as offering payment arrangements and remitting interest and any related penalties.

Despite these strategies, the ATO's approach to collecting debts has been a persistent cause of taxpayers' complaints, accounting for 23 per cent of all ATO-related complaints received by the Commonwealth Ombudsman in 2012–13.⁵³²

Similarly, during the consultation on the Inspector-General of Taxation's (IGT) 2014 work program, submissions particularly by individuals, small businesses, their advisers and representative bodies raised concerns with the ATO's approach to debt collection and the associated costs.

In submissions, stakeholders have asserted that the ATO has more recently taken a firmer approach to debt collection creating additional strain for taxpayers in continuing unfavourable economic conditions. Other stakeholders were of the opinion that the ATO allows debts to accumulate for too long before taking action. They have called for alternative approaches that seek to more effectively manage and reduce the level of overall debt, for example, by earlier and more frequent action which appropriately takes into account taxpayers' circumstances and compliance costs.

⁵²⁹ Australian Government, *Australian Taxation Office* <<http://australia.gov.au>>.

⁵³⁰ Australian Taxation Office (ATO), *Annual Report 2003-04* (2004) p 42; ATO, *Annual Report 2012-13* (2013) p 39.

⁵³¹ ATO, *Annual Report 2012-13* (2013) pp 35, 39-40.

⁵³² Commonwealth Ombudsman, *Ombudsman 2012-2013 Annual Report* (2013) p 56; Commonwealth Ombudsman, Submission No 1 to House of Representatives Standing Committee on Tax And Revenue, Parliament of Australia, *Inquiry into the Australian Taxation Office Annual Report 2012-13*, 31 January 2014, p 5.

Stakeholders have also questioned the efficiency and consistency of the ATO's debt recovery and assistance activities, including the reliance on the BVAT to inform such activities. Specifically, stakeholders have expressed that certain debt recovery activities were disproportionate and had broader impact. Examples of such activities included insolvency proceedings commenced against viable taxpayers, garnishee notices that exhausted bank accounts and concurrent debt recovery action which impedes challenges to the underlying assessments.

Certain ATO communications were also perceived to be ineffective or otherwise intimidating in relation to the potential consequences of non-payment and inadequate in terms of the potential ATO assistance which may be available to taxpayers to pay their debts.

Stakeholders have also made representations that some debt collection activities involved inaccurate ATO information and they faced difficulties in having such information corrected by the ATO. They have further asserted that the ATO may not be making the best use of information that is available to them from other sources such as the Australian Securities and Investments Commission.

Another major source of dissatisfaction for stakeholders was the ATO's use of EDCAs. Concerns were expressed that taxpayers were unable to engage with the ATO once a debt had been referred to an EDCA for recovery. The appropriateness of EDCAs' security arrangements for taxpayer information as well as the former's conduct and communication were also raised as concerns.

The IGT will conduct this review pursuant to subsection 8(1) of the *Inspector-General of Taxation Act 2003* (IGT Act) and welcomes your input. The following terms of reference and guidelines are provided to assist with the preparation of your submissions.

TERMS OF REFERENCE

The IGT review into the ATO's approach to debt collection will focus on:

1. *The ATO's strategies to manage tax debts, including those targeted at:*
 - a. *reducing the amount and age of total debt;*
 - b. *better managing compliance activities and disputes to facilitate expedited collection of undisputed debt;*
 - c. *accounting for and reporting on disputed debts; and*
 - d. *anticipating debts that are likely to arise and taking appropriate action to recover debt efficiently whilst being cognisant of taxpayers' circumstances.*
2. *The structure and design of the ATO's debt recovery and assistance initiatives.*
3. *The proportionality, consistency and effectiveness of the ATO's debt recovery activities, including its use of:*
 - a. *garnishee notices;*
 - b. *director penalty notices;*
 - c. *departure prohibition orders; and*
 - d. *insolvency actions.*
4. *The appropriateness and consistency of assistance that the ATO offers taxpayers including:*
 - a. *payment arrangements;*
 - b. *remission of interest and penalties;*
 - c. *debt release for serious financial hardship; and*
 - d. *decisions not to pursue tax debts.*
5. *The appropriateness and consistency of ATO communications regarding tax debts.*
6. *The accuracy of ATO information relied upon and the means to correct that information.*
7. *The ATO's use of third party debt collectors.*

The IGT may also examine other relevant concerns raised or potential improvements identified during the course of this review.

SUBMISSION GUIDELINES

We envisage that your submission will set out your experiences and views on the ATO's approach to managing tax debts.

It is important to provide detailed accounts of your experiences with the ATO approaches to managing tax debts which have had an impact on you. In this respect, it would be useful to provide a timeline of events outlining your key interactions with the ATO including key correspondence, the issuing of final notices and other ATO notices and the outcomes of any disputes. As far as possible, these approaches should address the terms of reference above.

In addition to your views on potential improvements, we are seeking examples of ATO approaches that have contributed to positive outcomes.

The following questions may assist you in your response.

The ATO's approach to managing tax debts

- Q1. What are your views on the ATO's approach to managing tax debts?
- Q2. How can the ATO better reduce the level of debt whilst taking into account taxpayers' circumstances and the broader economic impacts? Please explain your views.
- Q3. How can the ATO better anticipate debts that are likely to arise and what action should it take? Please explain your views.
- Q4. What factors do you think should be relevant for the ATO to consider when differentiating its debt collection recovery and assistance activities between taxpayers?
- Q5. Have you had experience with the ATO's debt collection activities (either as a taxpayer or as a representative of a taxpayer)? For example, garnishee notices, insolvency proceedings or director penalty notices. If so, please provide a detailed account of your experience, including:
 - a. a timeline of key events and a description of the actions taken by the ATO;
 - b. your views on whether these ATO actions were appropriate and commensurate with the circumstances and the risks to the revenue;
 - c. the impact that such action had on the taxpayer, its clients and creditors;
 - d. how effective was the ATO in communicating the tax debts and engaging throughout the process to understand the taxpayer's circumstances, such as engaging in alternative dispute resolution in relation to disputed debts;
 - e. how effective was the ATO in communicating the tax debts and engaging throughout the process to understand the taxpayer's circumstances, such as engaging in alternative dispute resolution in relation to disputed debts;

- f. the accuracy of the ATO's information regarding the tax debts and, if information was inaccurate, how the ATO resolved these inaccuracies; and
 - g. the nature of any assistance the ATO made available in paying the tax debts and how the ATO determined what assistance to provide (for example, payment arrangements, interest remission or debt release for serious financial hardship).
- Q6. If you were a creditor to a taxpayer who was subject to ATO debt collection activities, what was your experience? Please explain your views.
- Q7. If you are a tax practitioner, what are your views on the consistency with which the ATO collects debts and offers assistance? What are your views on the consistency with which the ATO's third party debt collectors collect tax debts?
- Q8. Do you have suggestions for how the ATO could improve its debt recovery and assistance processes? Please explain your suggestions.
- Q9. Have you had experience with a tax debt that was referred to a third party debt collector? If so, please provide a detailed account of your experience and your views on the matter, including:
 - a. their conduct in managing the matter;
 - b. the accuracy and security of information held about you; and
 - c. the nature of any interactions you had with the ATO at the same time.
- Q10. Do you have suggestions for improvement in relation to the ATO's arrangements with third party debt collectors and related debt recovery processes? Please explain your suggestions.

Other

- Q11. Are there any other areas on which you would like to make submissions? For example, you may wish to cite international experiences or comparisons which you believe would lead to improvements.

LODGMENT

The closing date for submissions is 18 July 2014. Submissions can be sent by:

Post to: Inspector-General of Taxation
 GPO Box 551
 SYDNEY NSW 2001

Email to: debt@igt.gov.au

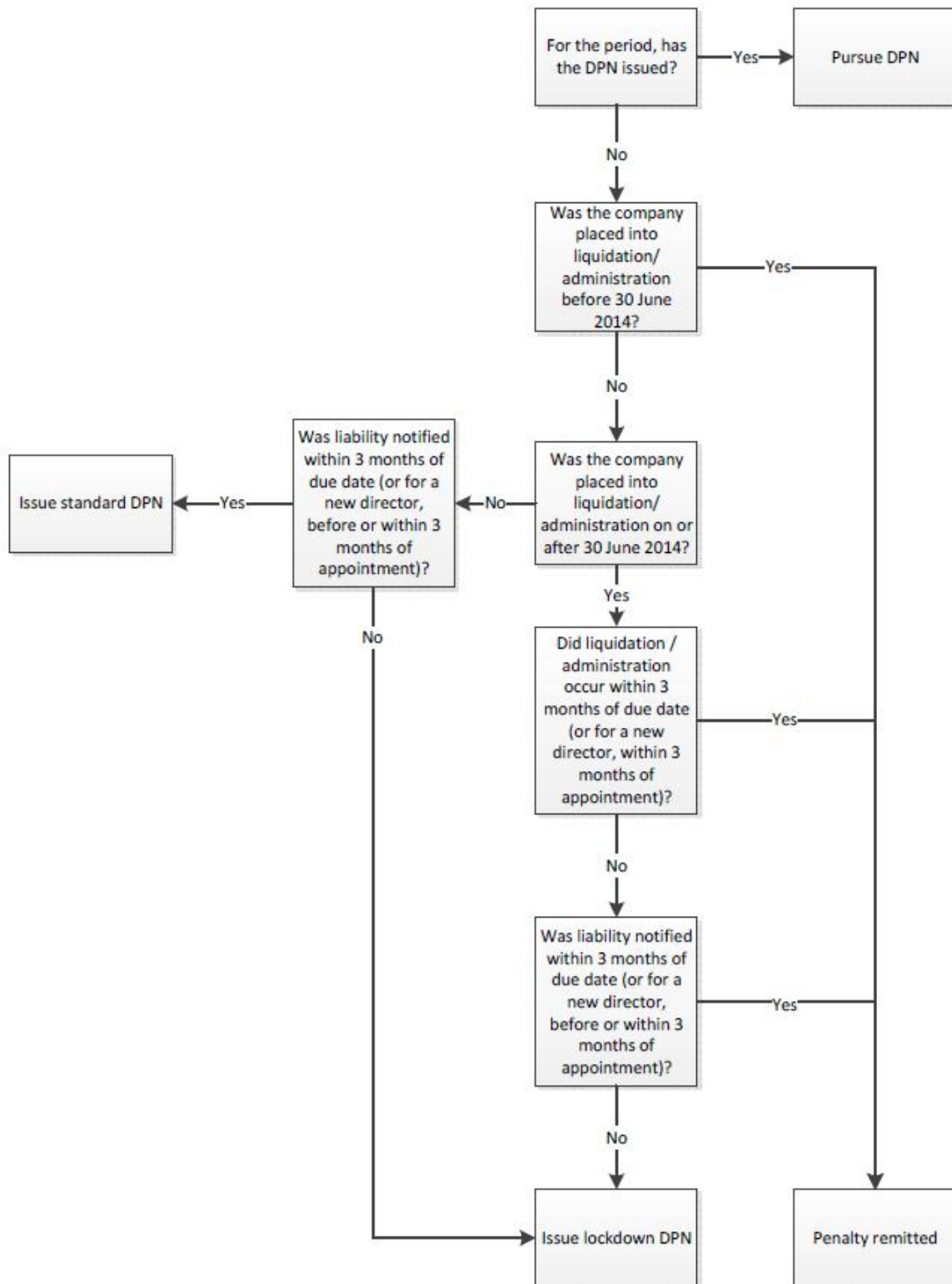
CONFIDENTIALITY

Submissions provided to the IGT are in strict confidence (unless you specify otherwise). This means that the identity of the taxpayer, the identity of the adviser and any information contained in such submissions will not be made available to any other person, including the ATO. Sections 23, 26 and 37 of the IGT Act safeguard the confidentiality and secrecy of such information provided to the IGT – for example, the IGT cannot disclose the information as a result of an FOI request, or as a result of a court order generally. Furthermore, if such information is the subject of client legal privilege (or legal professional privilege), disclosing that information to the IGT will **not** result in a waiver of that privilege.

APPENDIX 2: DIRECTOR PENALTY NOTICES

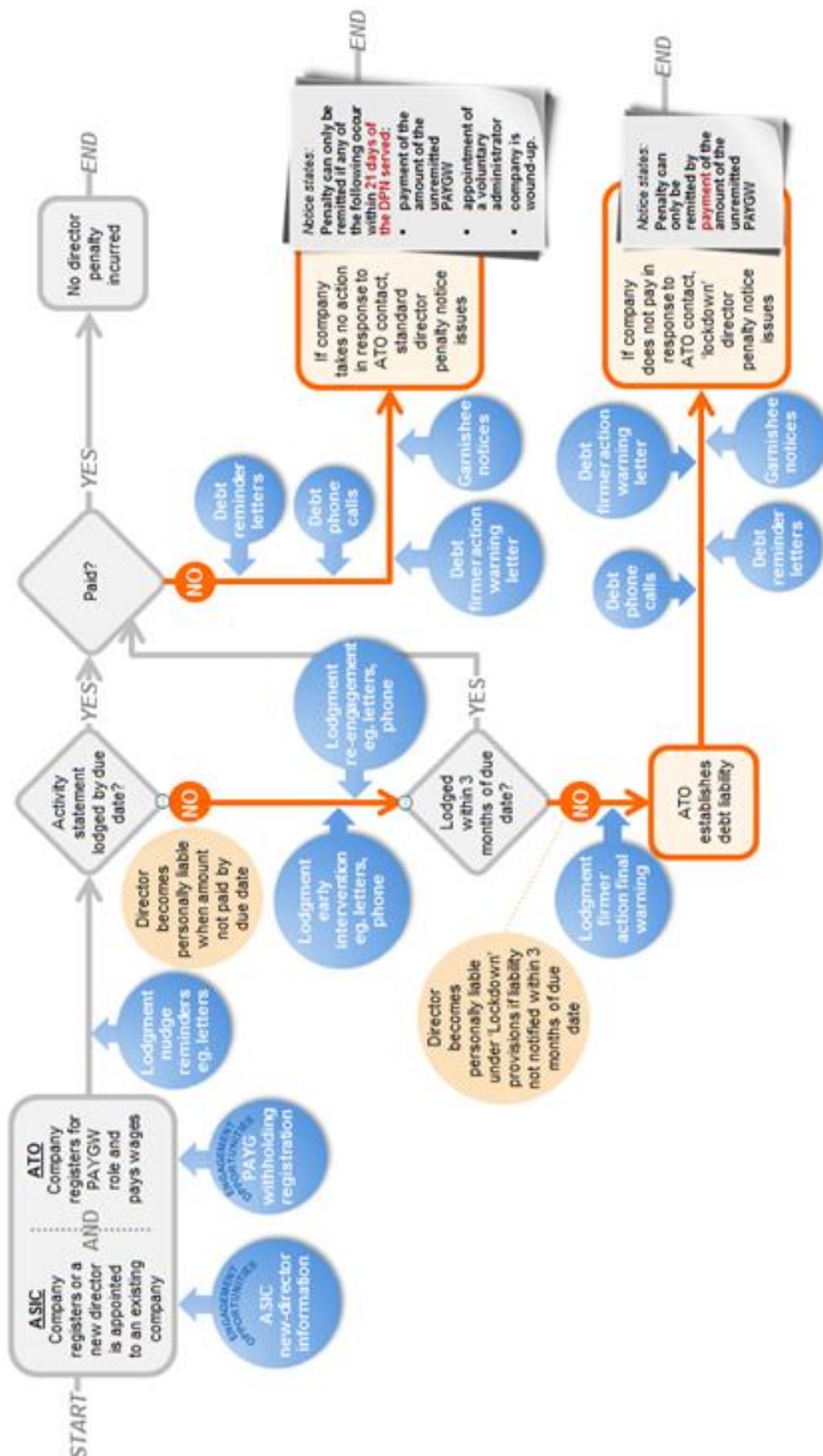
Figure A2.1: Selecting the type of DPN

Assumption: Actual PAYGW liability and for a period before any liquidation/administration



Source: ATO.

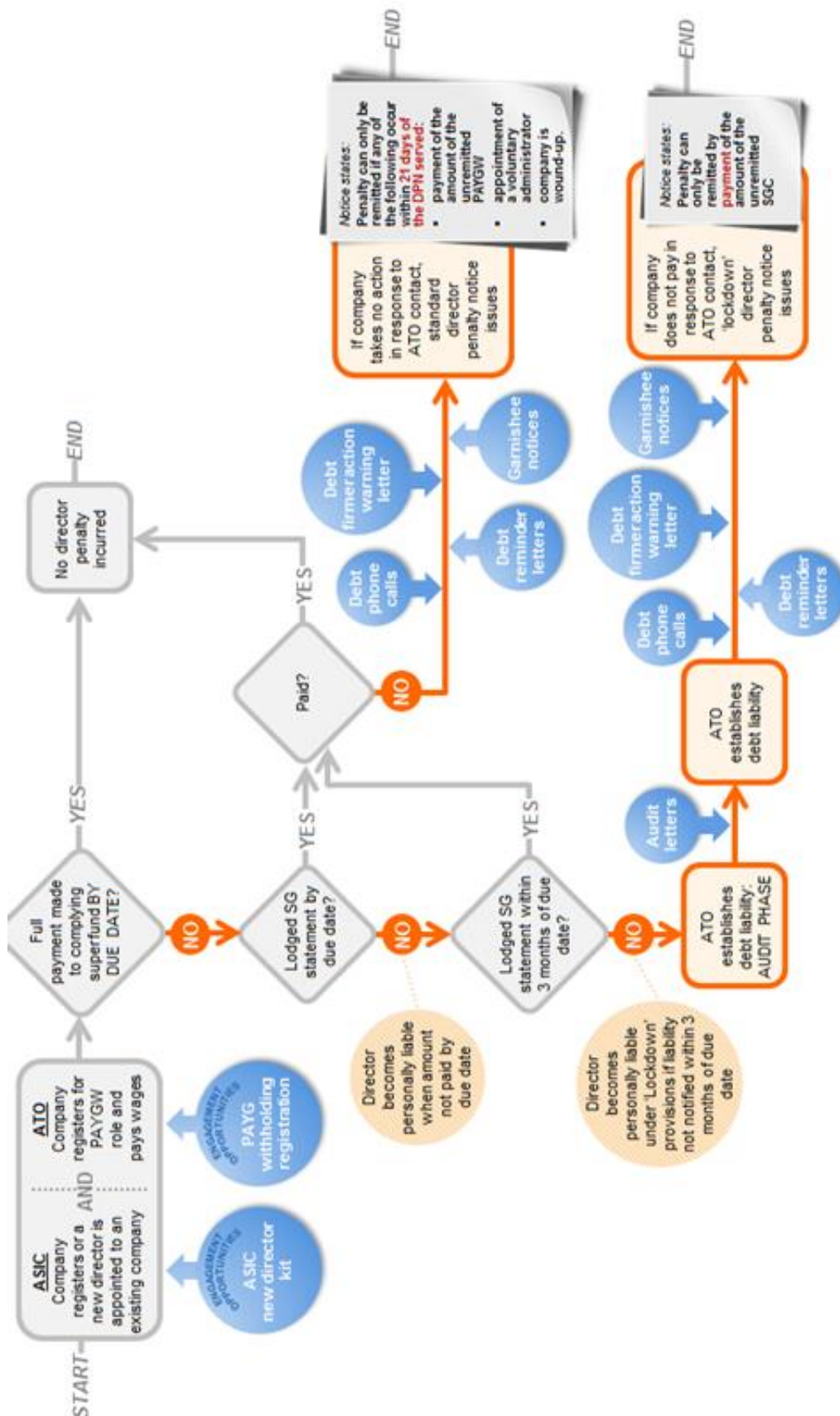
Figure A2.2: DPN for PAYG Withholding obligations



Source: ATO.

Note: Does not include obligations and timeframes for appointment of new directors to existing companies where, at the time of appointment, there is an outstanding SGC obligation.

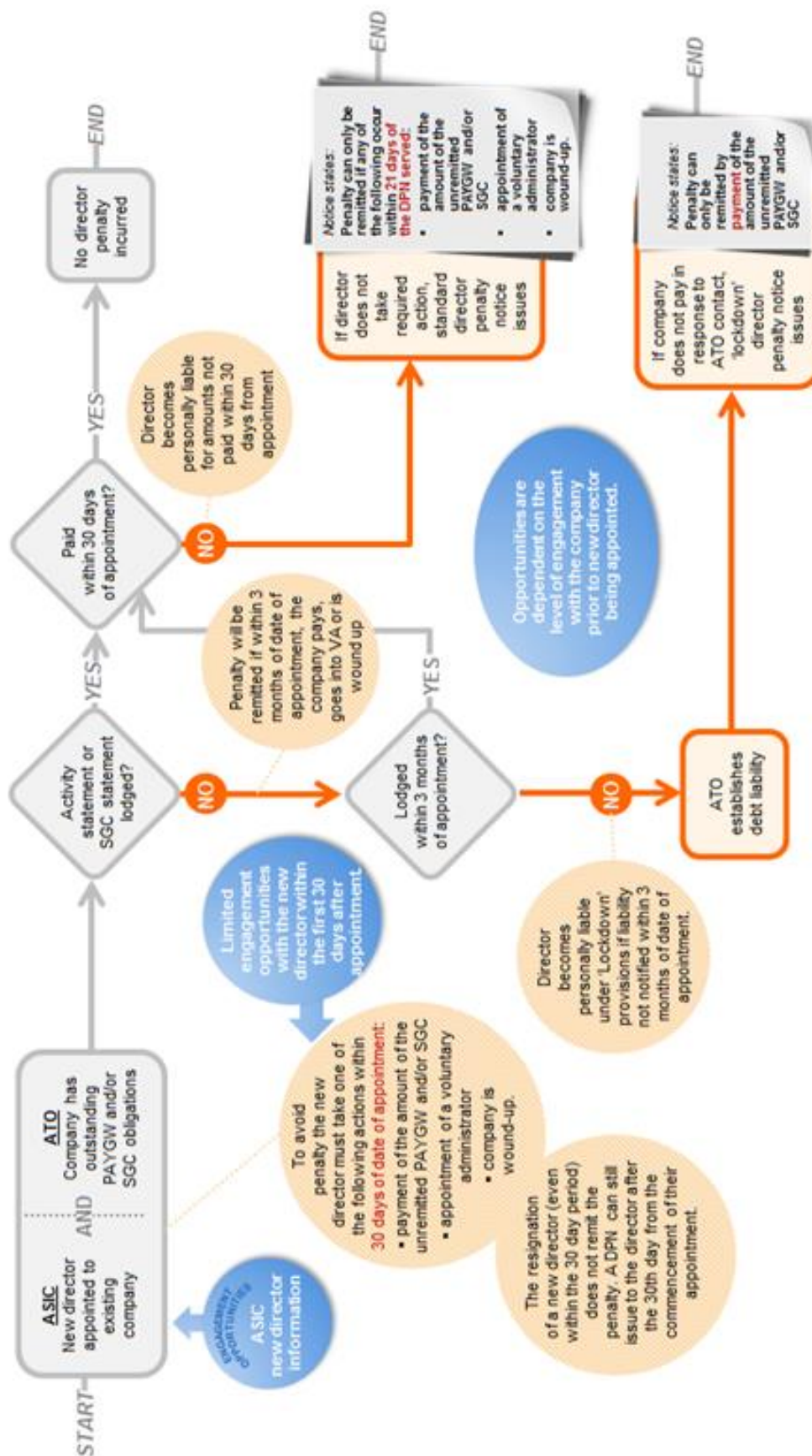
Figure A2.3: DPN for Superannuation Guarantee Charge obligations



Source: ATO.

Note: Does not include obligations and timeframes for appointment of new directors to existing companies where, at the time of appointment, there is an outstanding SGC obligation.

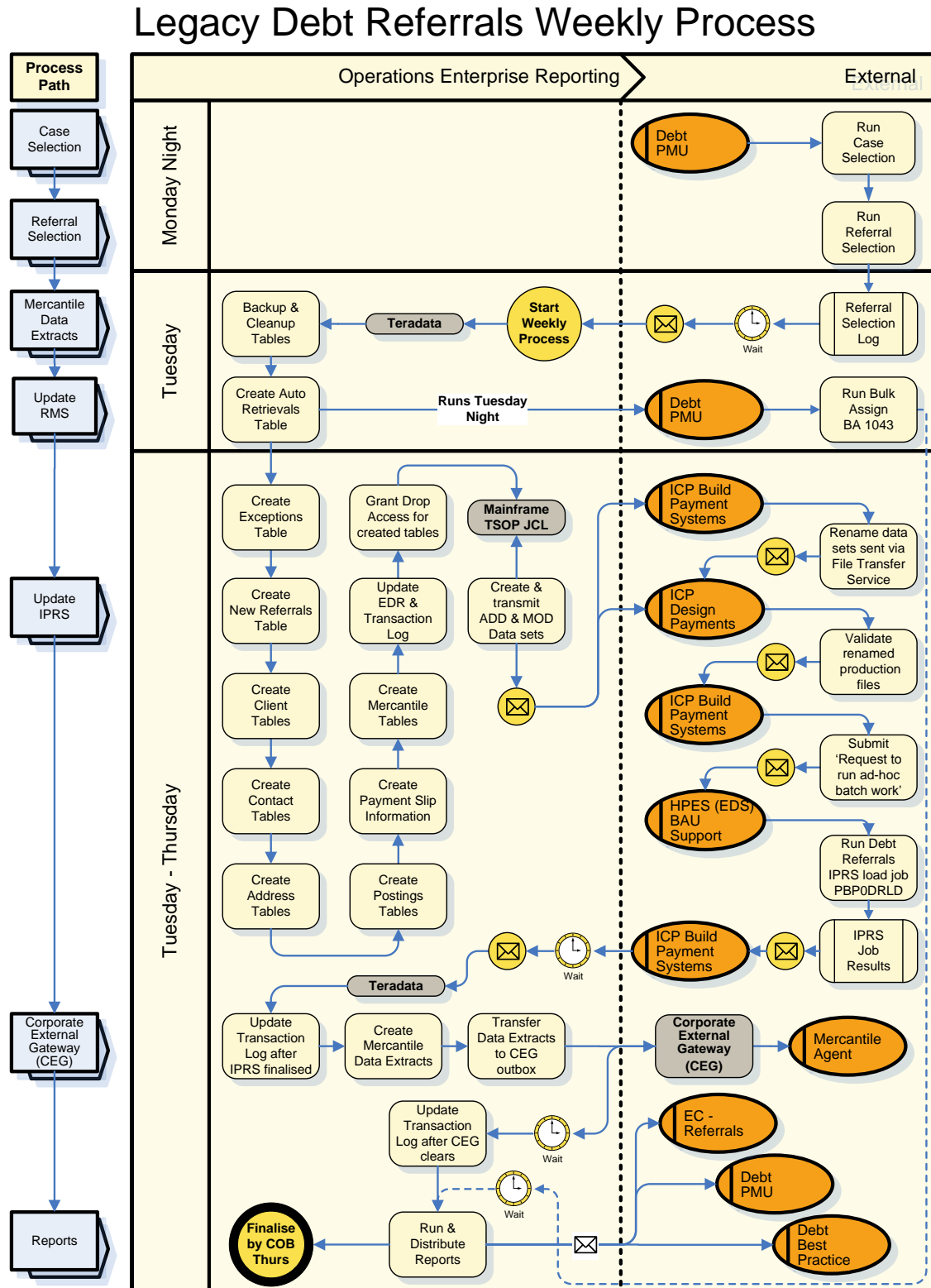
Figure A2.4: Director Penalty Notice for new directors where company has outstanding PAYG Withholding and/or Superannuation Guarantee Charge obligations



Source: ATO.

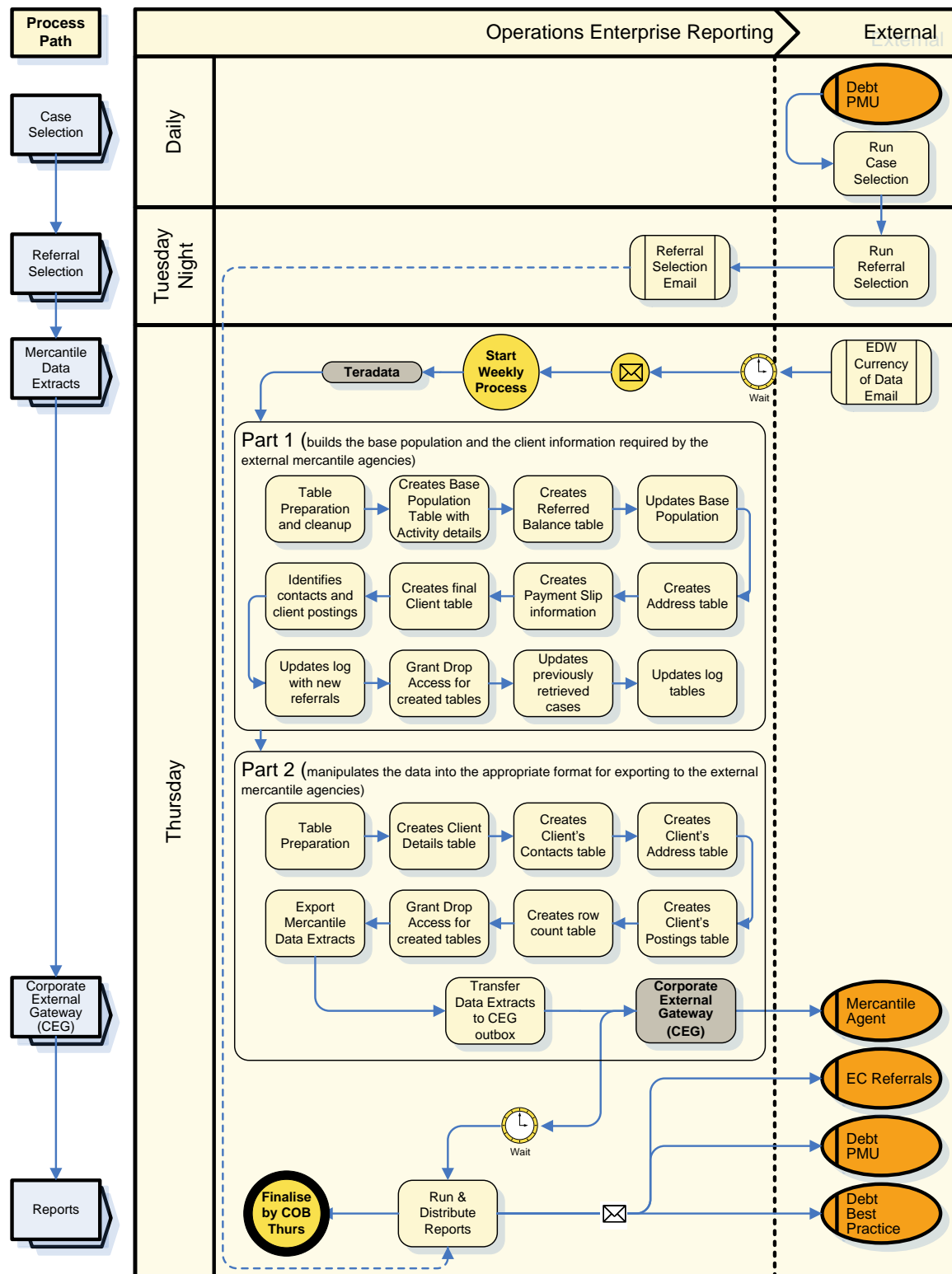
APPENDIX 3: EDCA WEEKLY TRANSMISSION PROCESS

Figure A3.1: Weekly Client Account Centre and Superannuation Guarantee Charge referral and retrieval process



Source: ATO.

Figure A3.2: Weekly income tax debt referral and retrieval process

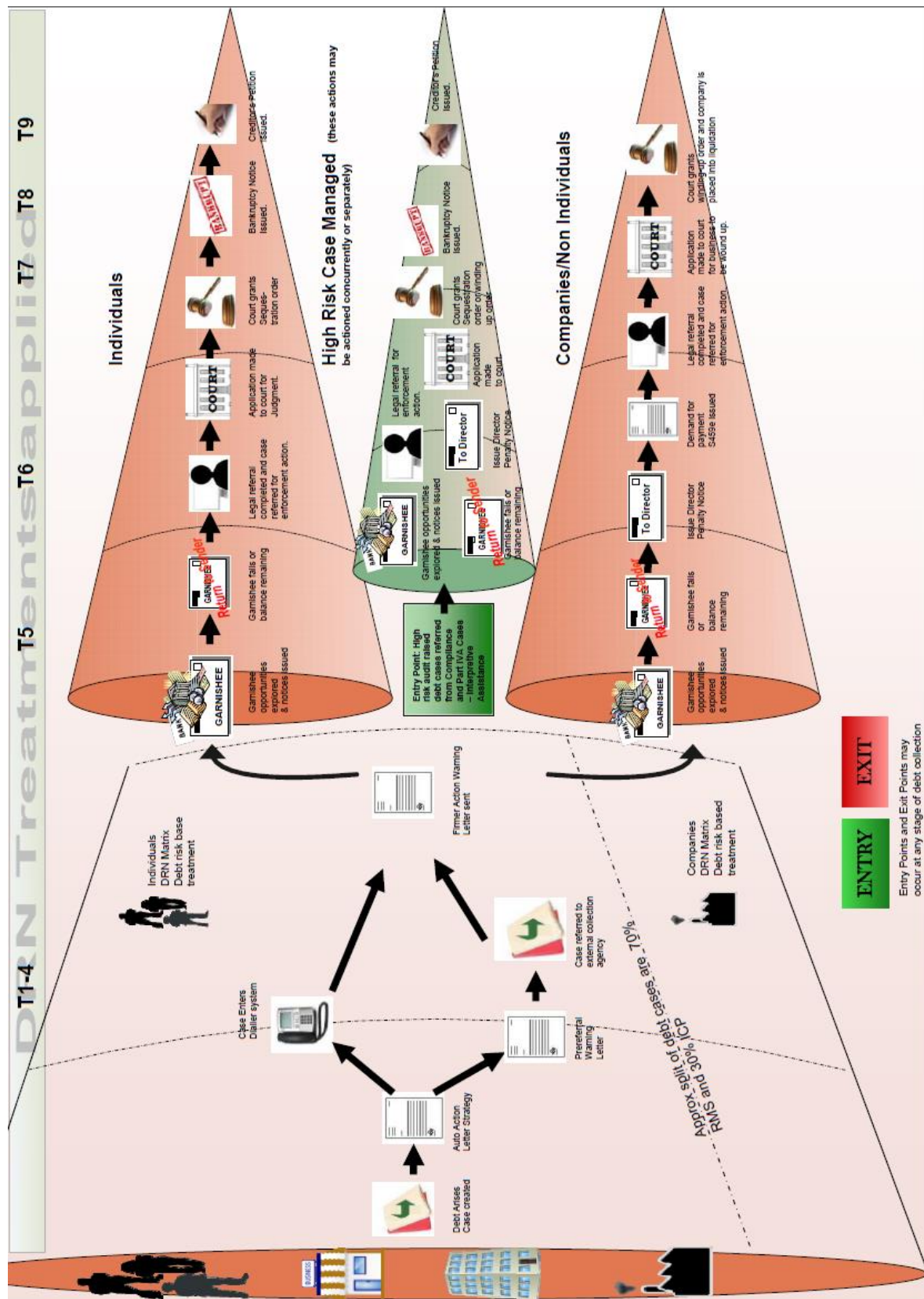


Version 1 - Friday, 21 June 2013

Source: ATO.

APPENDIX 4: DEBT RIGHT NOW PROGRAM

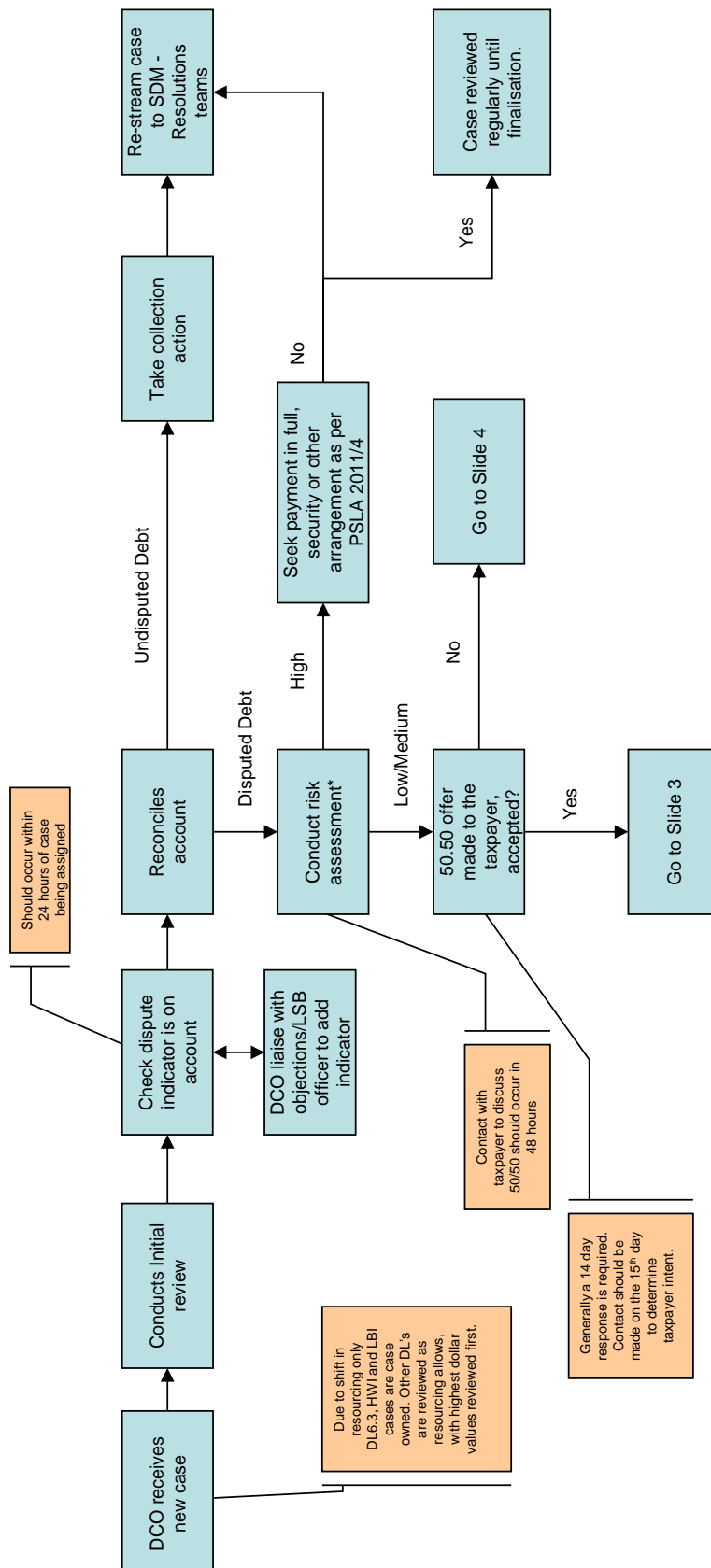
Figure A4.1: Debt case lifecycle



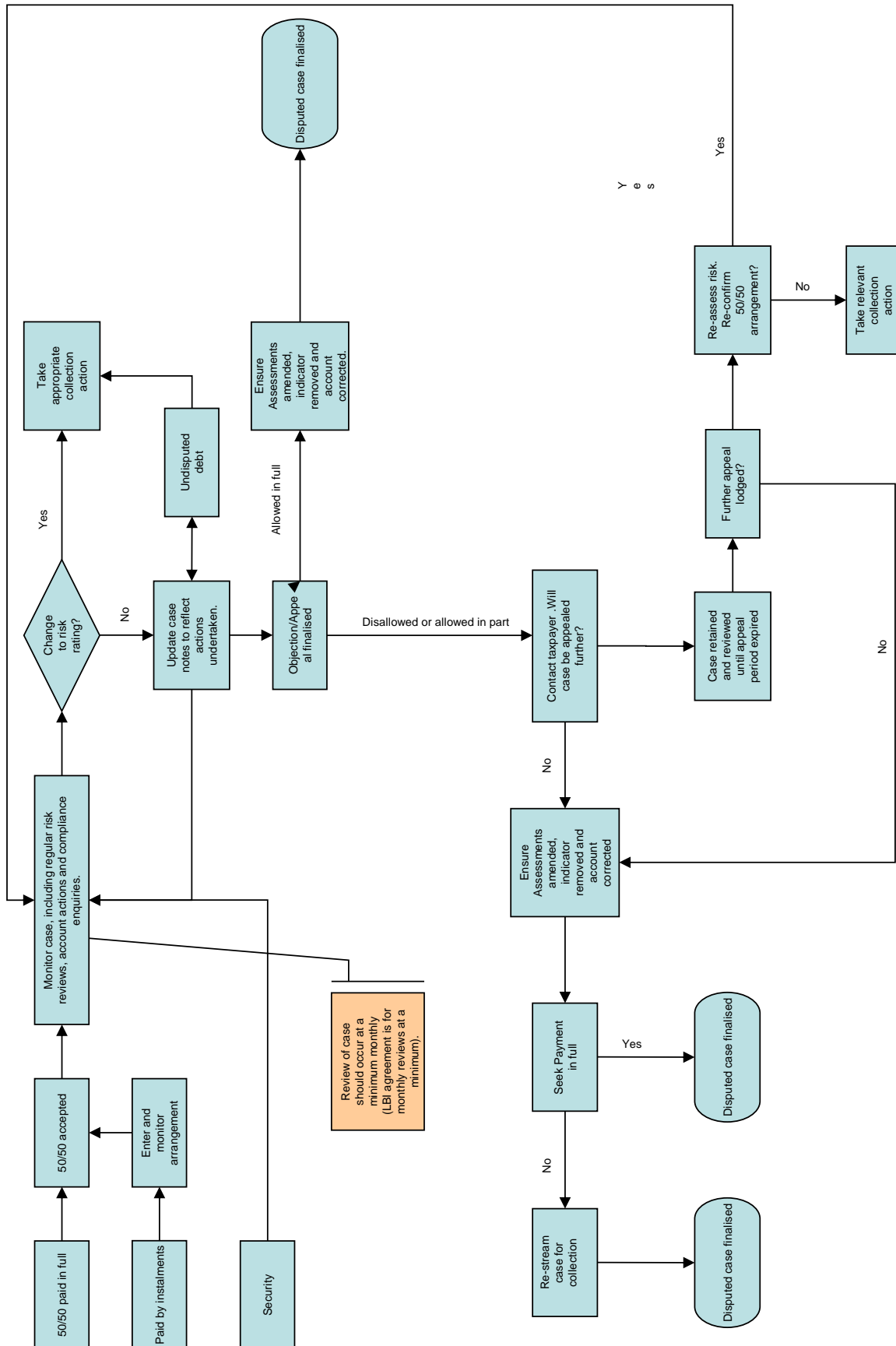
Source: ATO.

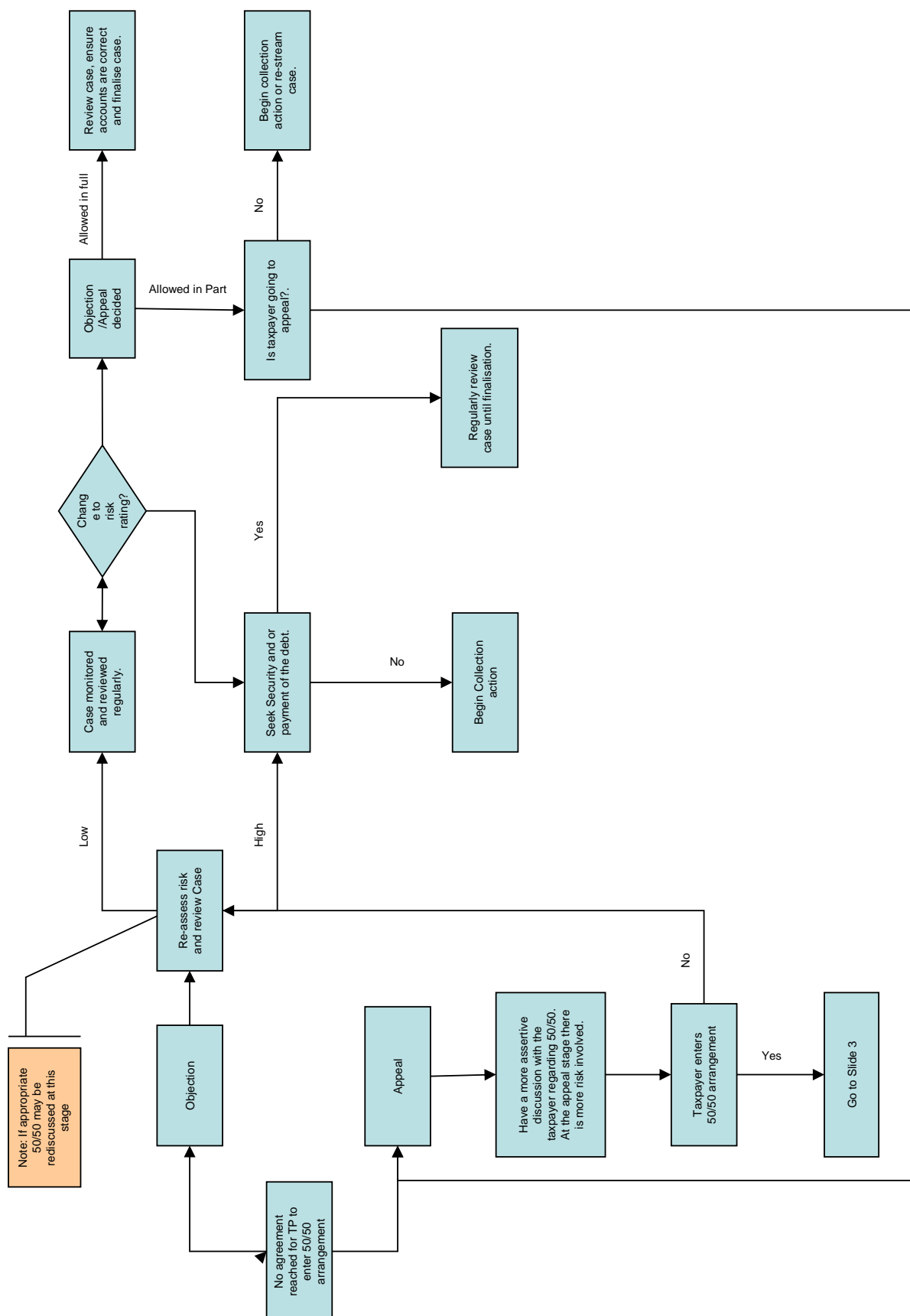
APPENDIX 5: DISPUTED DEBT 50/50 ARRANGEMENT

Figure A5.1: Disputed debt 50/50 arrangement



*There are rare situations where a 50:50 arrangement would be offered on higher risk cases. This would be if the potentially high risks of the case would be mitigated through the acceptance of a 50:50 arrangement. If the offer is not accepted then normal processes as per high risk would apply.





Source: ATO, 'Disputed Debt – End to End process' (Internal ATO document, undated).

APPENDIX 6: ATO DRAFT REVISED DEBT EFFECTIVENESS MEASURES

Table A6.1

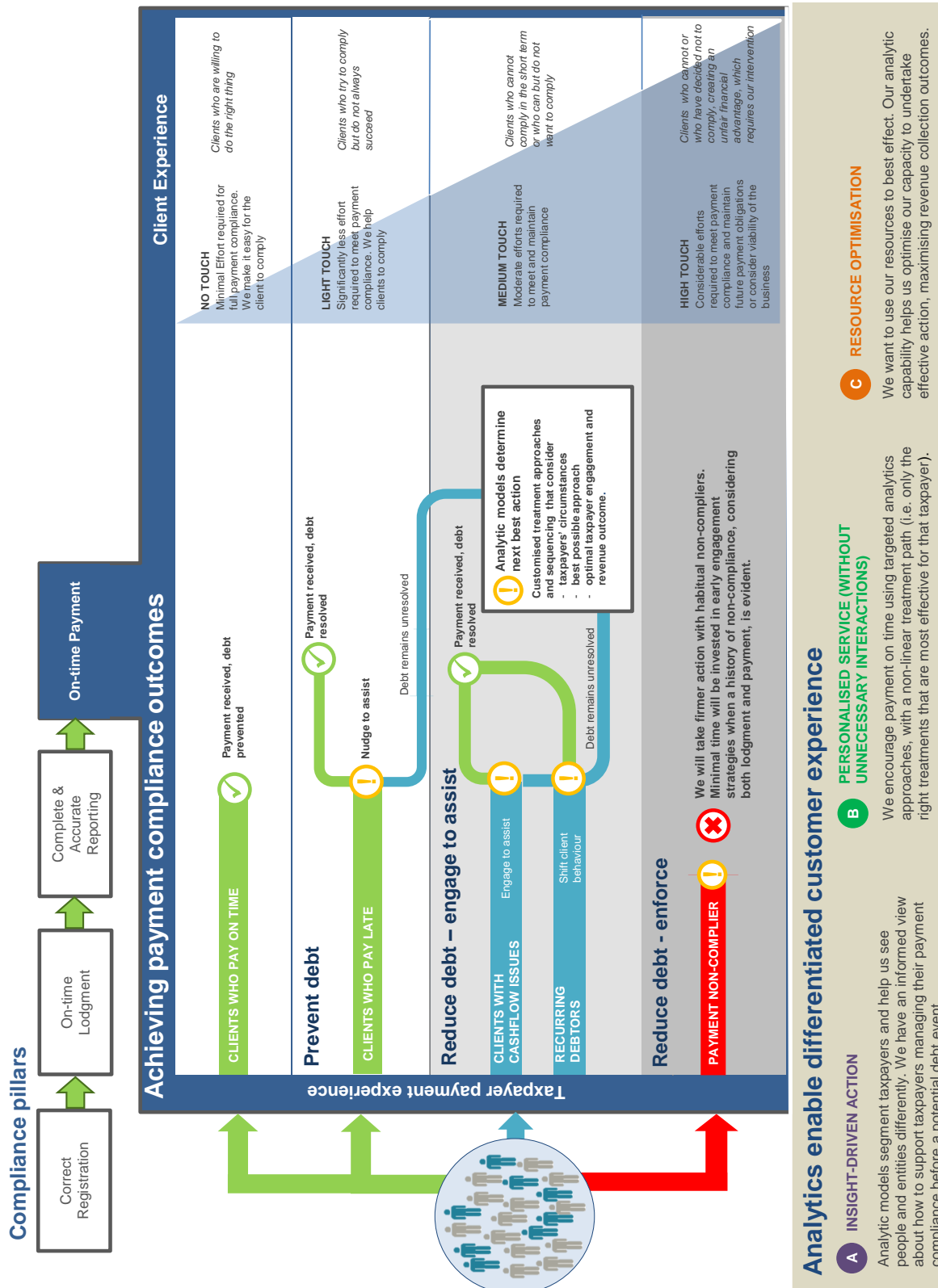
Strategic Outcomes	Enterprise Risks	Payment Compliance Outcomes	Debt's Overarching Strategies	Service Delivery Client Experience Continuum	High Level Performance Indicators
Revenue	ER19 (Level 0) - Tax Revenue ER Level 1 – Failure to maintain payment compliance at acceptable tolerance levels	Enforce	Improve payment over time through targeted risk differentiation and client engagement analytics	High Touch	<ol style="list-style-type: none"> 1. Payment on time (trend) <ul style="list-style-type: none"> ▪ Payment over time (including mix of self-finalisers and early intervention) (trend) 2. Trend in ratio of collectable debt to net/gross collections * (benchmark) 3. Trend in debt resolved attributed to our payment compliance activities (including self finalisers) 4. Inventory turnover 5. Proportion of impaired (bad and doubtful) debt to total tax receivables * (trend)
		Engage		Medium Touch	
Willing Participation		Prevent Debt	Improve payment on time through targeted risk differentiation and client engagement analytics	Light Touch / Nudge	<ol style="list-style-type: none"> 1. Payment on time (trend) <ul style="list-style-type: none"> ▪ Ratio of cash collections to compliance liabilities raised ▪ Ratio of cash collections to self-assessed liabilities 2. Prioritisation of the payment of tax liability 3. Effectiveness of behavioural interventions over time
				No Touch	

Strategic Outcomes	Enterprise Risks	Payment Compliance Outcomes	Debt's Overarching Strategies	High Level Performance Indicators
Integrity (Administration)	ER16 (Level 0) – Product and payment processing ER Level 1 – Failure to manage debt collection processes to agreed levels of performance and integrity	Easy for people to participate	Make it easier for people to participate	1. Trends in online self-service/channel shift 2. Community and stakeholder engagement and satisfaction with Debt performance ^a <ul style="list-style-type: none"> Payment thinking (respect, educate and inform, differentiate treatment based on willingness to comply, co-design solutions) (need to develop this indicator)
		Contemporary and tailored service		3. Performance against plan <ul style="list-style-type: none"> Risk, Strategy, Delivery plan Debt paid against collection forecast Holdings under active management compared with holdings which are not Workforce mix and skills view – plan/required/actual Right work for FTEs for best outcome
		Purposeful and respectful relationships	Strategic partnerships with key stakeholders for certain outcomes	4. Proportion of timely client initiated activities vs. ATO initiated activities
		Professional and productive organisation	Reinventing staff capability to build expertise	

Source: ATO.

APPENDIX 7: ANALYTICS FOR CLIENT ENGAGEMENT PROGRAM

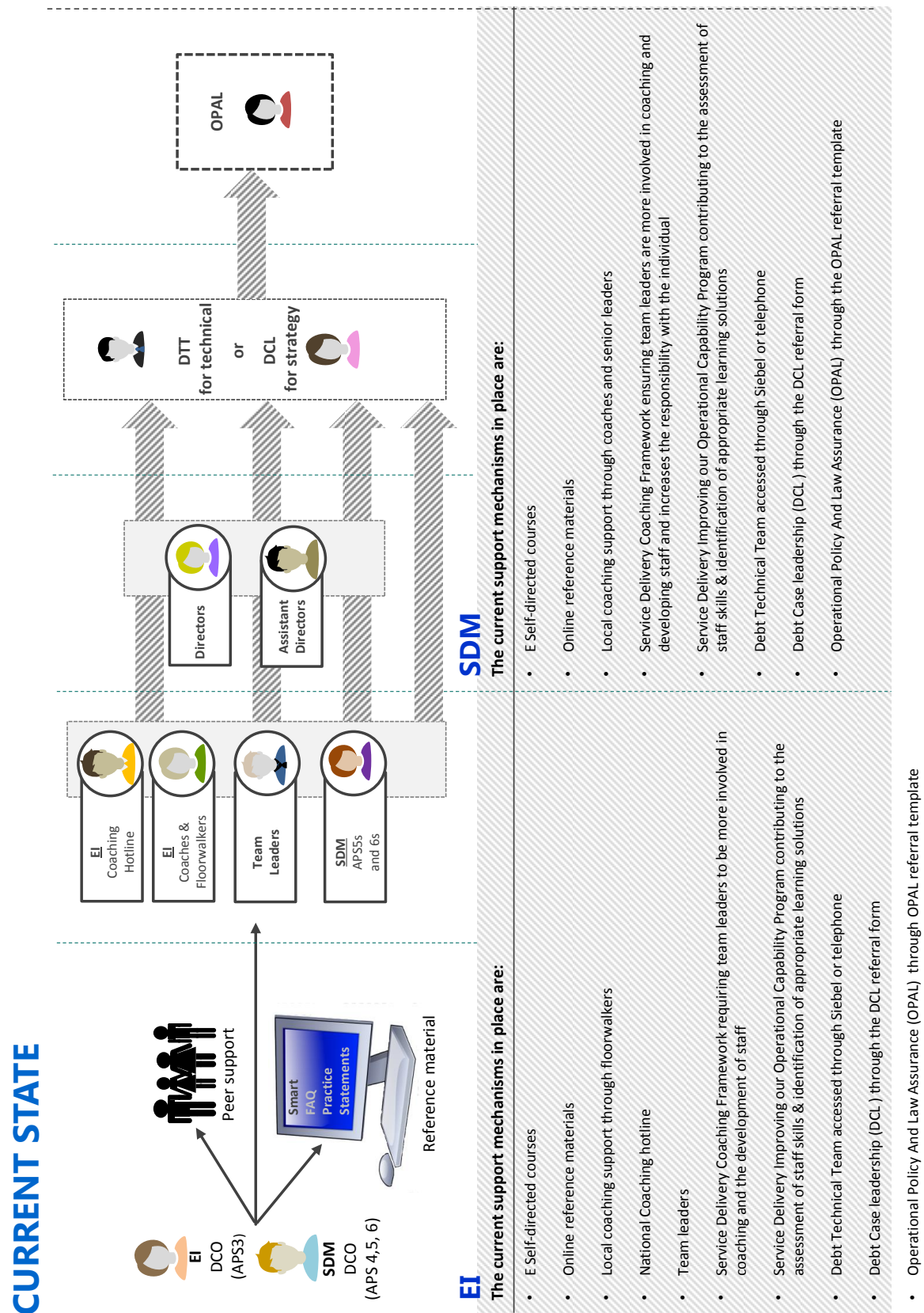
Figure A7.1: Analytics for Client Engagement Program



Source: ATO Communication to the IGT, 11 March 2015.

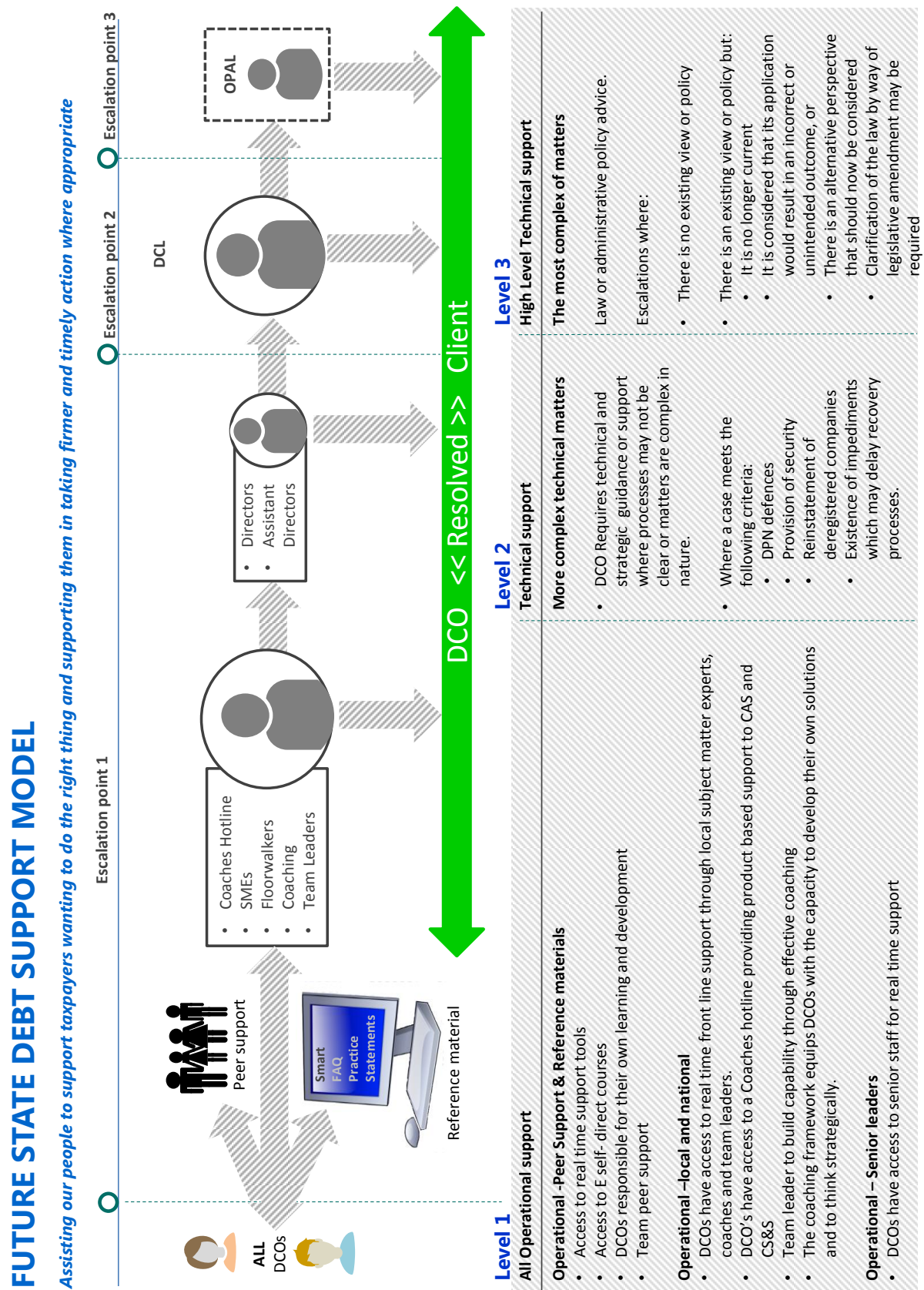
APPENDIX 8: DEBT STAFF SUPPORT MECHANISMS

Figure A8.1: Current debt support mechanisms



Source: ATO Communication to the IGT, 1 April 2015.

Figure A8.2: Future debt support mechanisms



Source: ATO Communication to the IGT, 1 April 2015.

APPENDIX 9: PAYMENT CHANNEL PROCESSING TIMES

Figure A9.1: processing times for various payment channels

Payment Channel Data/Funds Overview

This matrix uses the following definitions:
 Day 0 = day payment made (BPAY, Credit Card, Direct Credit), received (Mailpay, BillPay), or authorised to be deducted (Direct Debit)
 Day 1 = the 24 hour period following day zero
 Day 2 = the 24 hour period following day one

Inbound Payment Channel	What are the daily cut-off times when making/receiving a payment?	When are funds banked to an ATO bank account?	When is client account data received from external provider?	When does data report in GLIS?	When is data viewable in the IPRS Journal?	When is data viewable on client account?
BPAY	Day 0 Various. Depends on the client's financial institution cut-off time.	Day 0 PM Funds banked same day.	Day 1 AM Data sent from RBA overnight.	Day 1 PM Data loads to GLIS in the afternoon.	Day 1 PM Data load begins at 7.00pm daily.	ICP – Day 1 after 5.30pm Legacy – Day 2 7 am or after the accounting batch processes have run
CREDIT CARD	Day 0 Service accepts payments up to 6pm Sydney time.	Day 0 PM Funds banked same day.	Day 1 AM Data sent from RBA overnight.	Day 1 PM Data loads to GLIS in the afternoon.	Day 1 PM Data load begins at 7.00pm daily.	ICP – Day 1 after 5.30pm Legacy – Day 2 7 am or after the accounting batch processes have run
DIRECT CREDIT	Day 0 Various. Depends on the client's financial institution cut-off time.	Day 0 PM Funds banked same day.	Day 1 AM Data sent from RBA overnight.	Day 1 PM Data loads to GLIS in the afternoon.	Day 1 PM Data load begins at 7.00pm daily.	ICP – Day 1 after 5.30pm Legacy – Day 2 7 am or after the accounting batch processes have run
DIRECT DEBIT (Legacy)	Day 0 ATO provides details to RBA to debit client's financial institution.	Day 0 PM Funds banked same day.	Day 0 ATO creates own data as a result of RBA file acknowledgment, which includes any rejects. Dishonour data sent from RBA over next few days.	Day 0 PM Data loads to GLIS in the afternoon.	Day 0 PM Data load begins at 7.00pm daily.	Day 1 7 am or after the accounting batch processes have run
DIRECT DEBIT (ICP)	Day 0 AM ATO provides details to RBA to debit client's financial institution.	Day 0 PM Funds banked same day.	Day 0 AM ATO creates own data. Reject data sent from RBA Day 0 PM. Dishonour data sent from RBA over next few days.	N/A ICP direct debit data does not load to GLIS.	N/A ICP direct debit data does not load to IPRS.	Day 0 AM Payment form created when Direct Debit process runs.
BILLPAY	Day 0 Up to post office closing times.	Day 0, 1, 2, 2+ Funds banked progressively over a few days.	Day 1 AM Data sent from AP overnight.	Day 1 PM Data loads to GLIS in the afternoon.	Day 1 PM Data load begins at 7.00pm daily.	ICP – Day 1 after 5.30pm Legacy – Day 2 7 am or after the accounting batch processes have run
MAILPAY	Day 0 Refers to cheques being a 'clean-skin' ready for processing. Cheques will be processed up to approx 3pm.	Day 0 & 1 Funds banked same day for EP cheques. Next day banking for non EP cheques.	Day 0 PM IPPS creates own data and this is ready after 'end day' processes.	Day 0 PM Data loads to GLIS in the afternoon.	Day 0 PM Data load begins at 7.00pm daily.	ICP – Day 0 after 5.30pm Legacy – Day 1 7 am or after the accounting batch processes have run

** Refers to 'clean-skin' data only. Some payment data received in error can be held in the IPRS Error Queue for varying periods of time. Data is visible in IPRS and on the client account when the error is corrected.

Source: ATO Communication to the IGT, 6 March 2015.

APPENDIX 10: ATO RESPONSE



Australian Government
Australian Taxation Office

Second Commissioner of Taxation

Mr Ali Noroozi
Inspector-General of Taxation
GPO Box 551
Sydney NSW 2001

18 June 2015

Dear Ali

Review into the Australian Taxation Office's approach to debt collection

Thank you for the opportunity to comment on your draft report into the ATO's approach to debt collection.

The ATO agrees in full, in part or in principle to sixteen of the nineteen recommendations. Our detailed response to all of the recommendations is attached at Annexure 1.

In agreeing to these recommendations, the ATO notes your recognition that the management of debt by the ATO requires balancing the need between support and assistance for individuals and businesses experiencing difficult circumstances, with the consistent and fair treatment of those who are not meeting their taxation obligations.

The ATO's new Debt strategy will strengthen this approach, by continuing to make it as easy as possible to pay, while ensuring those who fail to comply or choose not to work with us to meet their obligations, do not gain an unfair financial advantage over those who do. While the ATO is cognisant of the potentially sensitive impacts this strategy may have on businesses operating at the margins of solvency, we consider such an approach directly supports the integrity of the tax system and protects businesses that would otherwise be adversely impacted by the negative trading effects of poorly performing businesses.

While I had anticipated that the report may surface more transformational recommendations to help us enhance the Reinvention journey currently underway, I am pleased the report and recommendations support the overall direction of the ATO's Reinvention. Furthermore, I have noted that we have a range of initiatives and programs of work, already in place or underway in the ATO, that addresses a number of your recommendations.

The recommendations we have agreed to, support the ATO's previously announced shift in our approach to debt management - a shift strongly influenced by community feedback and increasing levels of debt in recent years, and underpinned by external research and advanced analytics. Our aim is to take the right treatment, at the right time, for the right taxpayer using the right ATO capability. This 'next best action' approach sees us also adopting a more preventative and contemporary approach to make it easier to pay and harder not to, including the use of simple tailored SMS reminder messages.

Other recommendations agreed to complement the intent of the ATO's Reinvention blueprint including building a professional workforce, integrated digital solutions and products and services that meet client needs, measuring and reporting on what is valued by the government and the community and providing certainty to taxpayers.

We disagree in full with only two recommendations, 4.5 and 4.7, and consider that Recommendation 3.3 is a matter for government to consider.

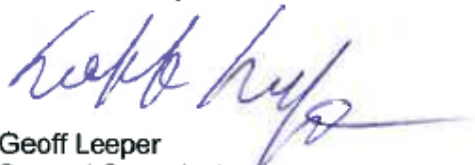
We have disagreed with Recommendation 4.5 as we are satisfied the current process of advising taxpayers whether or not we intend to offset credits against their overdue debts, both verbally and in writing, and gain agreement to this as a condition of their payment arrangement, is appropriate.

We have also disagreed with Recommendation 4.7 as we cannot pre-empt how the ATO should be structured in order to achieve our Reinvention blueprint outcomes.

The ATO has welcomed the open and constructive dialogue with you and your office over the course of the review. We trust that our interaction and feedback has contributed in a positive way to the final outcome.

If you or your officers have any further questions as you now work to finalise the report, please do not hesitate to contact me or our coordination team for the review (Thomas Ryan and Tracy Procter) or the External Scrutineers (Peter Coakley and Tig Hall).

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Geoff Leeper', with a long horizontal flourish extending to the right.

Geoff Leeper
Second Commissioner
Australian Taxation Office

[To minimise space, the annexure to the ATO's response has not been reproduced here, but has been inserted into the text of this report underneath each of the recommendations to which that text relates.]

SHORTENED FORMS

AAT	Administrative Appeals Tribunal
ACE	Analytics for Client Engagement
AFSA	Australian Financial Security Authority
AIS	ATO Integrated System
APS	Australian Public Service
ASBC	Australian Small Business Commissioner
ASIC	Australia Securities and Investments Commission
ATO	Australian Taxation Office
BAS	Business Activity Statement
BRP	Attitudinal and Behavioural Research on the Prevention of Aged Debt Project
BVAT	Business Viability Assessment Tool
C2P	Capacity to Pay Model
Commissioner	Commissioner of Taxation
CS&S	Customer Services and Support
D&B	Dun and Bradstreet
DAC	Departure Authorisation Certificate
DBL	Debt Business Line
DCL	Debt Case Leadership
DOCA	Deed of Company Arrangement
DOSO	Deed of Standing Arrangement
DPN	Director Penalty Notice
DPO	Departure Prohibition Order
DR Manual	Debt Reference Manual
DRN	Debt Right Now
DSRT	Debt Support Recovery Team
DST	Debt Serviceability Tool
EDCA	External Debt Collection Agency
EI	Early Intervention
FAW	Firmer Action Warning
Federal Court	Federal Court of Australia
FTL	Failure to Lodge
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GIC	General Interest Charge

GST	Goods and Services Tax
HMRC	Her Majesty's Revenue and Customs
IAS	Instalment Activity Statement
ICP	Integrated Core Processing
ICT	Information and Communication Technology
IGT	Inspector-General of Taxation
IRD	Inland Revenue Department
IRS	Internal Revenue Service
IVA	Independent Viability Assessment
IVR	Interactive Voice Response
KPI	Key Performance Indicator
LD&P	Law Design and Practice Group
NILA	Notice of Intended Legal Action
NOA	Notice of Assessment
OECD	Organisation for Economic Co-operation and Development
P2P	Propensity to Pay
PAYG	Pay As You Go
PBR	Performance Base Referral
PRWL	Pre-Referral Warning Letter
RBA	Running Balance Account
RDF	Risk Differentiation Framework
RDR	Review and Dispute Resolution
RMS	Receivables Management System
SDSP	Service Delivery Sub-plan
SDM	Significant Debt Management
SDQMS	Service Delivery Quality Management System
SES	Senior Executive Service
SGC	Superannuation Guarantee Charge
SLA	Service Level Agreement
SMART	Script Manager and Reference Tool
SME	Small to Medium Enterprises
TAA 1953	<i>Taxation Administration Act 1953</i>
TFN	Tax File Number